

# ARMSTRONG WORLD INDUSTRIES INC

## FORM 10-K (Annual Report)

Filed 02/26/09 for the Period Ending 12/31/08

Address	2500 COLUMBIA AVE LANCASTER, PA 17603
Telephone	7173970611
CIK	0000007431
Symbol	AWI
SIC Code	3089 - Plastics Products, Not Elsewhere Classified
Industry	Constr. - Supplies & Fixtures
Sector	Capital Goods
Fiscal Year	12/31

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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2008

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

**ARMSTRONG WORLD INDUSTRIES, INC.**

(Exact name of registrant as specified in its charter)

Pennsylvania (State or other jurisdiction of incorporation or organization)	1-2116 Commission file number	23-0366390 (I.R.S. Employer Identification No.)
P. O. Box 3001, Lancaster, Pennsylvania (Address of principal executive offices)		17604 (Zip Code)

Registrant's telephone number, including area code (717) 397-0611

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

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

Title of each class  
Common Stock (\$0.01 par value)

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

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

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes  No

The aggregate market value of the Common Stock of Armstrong World Industries, Inc. held by non-affiliates based on the closing price (\$29.22 per share) on the New York Stock Exchange (trading symbol AWI) on June 30, 2008 was approximately \$580 million. As of February 19, 2009, the number of shares outstanding of registrant's Common Stock was 57,039,580.

### Documents Incorporated by Reference

None

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### **Uncertainties Affecting Forward-Looking Statements**

Our disclosures here and in other public documents and comments contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act. Those statements provide our future expectations or forecasts, and can be identified by our use of words such as “anticipate,” “estimate,” “expect,” “project,” “intend,” “plan,” “believe,” “outlook,” etc. in discussions of future operating or financial performance, the outcome of contingencies such as liabilities or legal proceedings, or our ability to pay any dividends or take any particular corporate action.

Any of our forward-looking statements may turn out to be wrong. Our actual future results, or our ability to pay a dividend or take any particular corporate action, may differ materially from our expected results. Forward-looking statements involve risks and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future. We undertake no obligation to update any forward-looking statement.

You should take into account risks and uncertainties that affect our business, operations and financial condition in evaluating any investment decision involving Armstrong. It is not possible to predict all factors that could cause actual results to differ materially from expected and historical results. The discussion in the “Risk Factors” section below at Item 1A is a summary of what we currently believe to be our most significant risk factors. Related disclosures in subsequent 10-K, 10-Q and 8-K reports should also be consulted.

PART I

**ITEM 1. BUSINESS**

Armstrong World Industries, Inc. (“AWI” or “the Company”) is a Pennsylvania corporation incorporated in 1891. We are a leading global producer of flooring products and ceiling systems for use primarily in the construction and renovation of commercial, institutional and residential buildings. Through our United States (“U.S.”) operations and U.S. and international subsidiaries, we design, manufacture and sell flooring products (primarily resilient and wood flooring) and ceiling systems (primarily mineral fiber, fiberglass and metal) around the world. We also design, manufacture and sell kitchen and bathroom cabinets in the U.S.

Our business strategy focuses on providing value to customers through product innovation, product quality and customer service. In our businesses, these factors are the primary determinants of market share gain or loss. Our objective is to ensure that anyone buying a hard surface floor or ceiling can find an Armstrong product that meets his or her needs. Our cabinet strategy is more focused – on stock cabinets in select geographic markets. In these segments, we have the same objectives: high quality, good customer service and products that meet our customers’ needs. Our markets are very competitive, which limits our pricing flexibility. This requires that we increase our productivity each year – both in our plants and in our administration of the businesses.

We maintain a website at <http://www.armstrong.com>. Information contained on our website is not incorporated into this document. Annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, all amendments to those reports and other information about us are available free of charge through this website as soon as reasonably practicable after the reports are electronically filed with the Securities and Exchange Commission (“SEC”). These materials are also available from the SEC’s website at [www.sec.gov](http://www.sec.gov).

On December 6, 2000, AWI filed a voluntary petition for relief under Chapter 11 of the U.S. Bankruptcy Code in order to use the court-supervised reorganization process to achieve a resolution of AWI’s asbestos-related liability. On October 2, 2006, AWI’s plan of reorganization (the “POR”), as confirmed by the U.S. District Court for the District of Delaware by order dated August 18, 2006, became effective, and AWI emerged from Chapter 11. See Note 1 to the Consolidated Financial Statements for additional information about AWI’s Chapter 11 case.

In connection with its emergence from bankruptcy on October 2, 2006 (the “Effective Date”), AWI adopted fresh-start reporting in accordance with AICPA Statement of Position 90-7, “Financial Reporting by Entities in Reorganization under the Bankruptcy Code” (“SOP 90-7”). Adopting fresh-start reporting has resulted in material adjustments to the historical carrying amount of reorganized Armstrong’s assets and liabilities. See Note 3 to the Consolidated Financial Statements for more information. As a result, our post-emergence financial statements are not comparable to our pre-emergence financial statements. Despite the lack of comparability, we have combined the 2006 results of the Predecessor Company (which represent the first nine months of 2006 and include the impact of emergence) with the results of the Successor Company (which represent the last three months of 2006) to facilitate the year-to-year discussion of operating results in certain sections of this Form 10-K. The combined financial information for 2006 is merely cumulative and does not give pro forma effect to the Predecessor’s results as if the consummation of the POR and the related fresh-start reporting and other adjustments had occurred at the beginning of the period presented. Combining pre-emergence and post-emergence results is not in accordance with U.S. generally accepted accounting principles (“GAAP”).



## **Reportable Segments**

*Resilient Flooring* – produces and sources a broad range of floor coverings primarily for homes and commercial and institutional buildings. Manufactured products in this segment include vinyl sheet, vinyl tile and linoleum flooring. In addition, our Resilient Flooring segment sources and sells laminate flooring products, ceramic tile products, adhesives, installation and maintenance materials and accessories. Resilient Flooring products are offered in a wide variety of types, designs and colors. We sell these products worldwide to wholesalers, large home centers, retailers, contractors and to the manufactured homes industry.

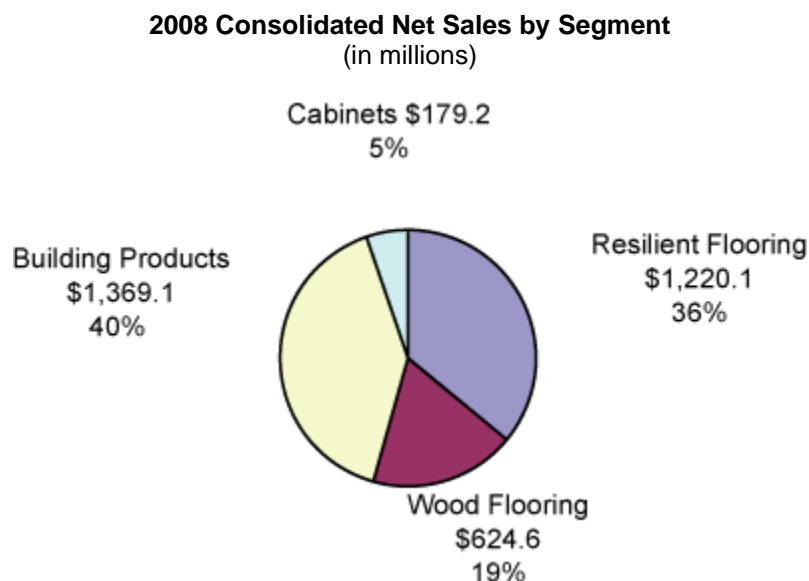
*Wood Flooring* – produces and sources wood flooring products for use in new residential construction and renovation, with some commercial applications in stores, restaurants and high-end offices. The product offering includes pre-finished solid and engineered wood floors in various wood species, and related accessories. Virtually all of our Wood Flooring sales are in North America. Our Wood Flooring products are generally sold to independent wholesale flooring distributors and large home centers. Our products are principally sold under the brand names Bruce<sup>®</sup>, Hartco<sup>®</sup>, Robbins<sup>®</sup>, Timberland<sup>®</sup>, Armstrong<sup>®</sup>, HomerWood<sup>®</sup> and Capella<sup>®</sup>.

*Building Products* – produces suspended mineral fiber, soft fiber and metal ceiling systems for use in commercial, institutional and residential settings. In addition, our Building Products segment sources complementary ceiling products. Our products, which are sold worldwide, are available in numerous colors, performance characteristics and designs, and offer attributes such as acoustical control, rated fire protection and aesthetic appeal. Commercial ceiling materials and accessories are sold to ceiling systems contractors and to resale distributors. Residential ceiling products are sold primarily in North America to wholesalers and retailers (including large home centers). Suspension system (grid) products manufactured by Worthington Armstrong Venture (“WAVE”) are sold by both Armstrong and our WAVE joint venture.

*Cabinets* – produces kitchen and bathroom cabinetry and related products, which are used primarily in the U.S. residential new construction and renovation markets. Through our system of Company-owned and independent distribution centers and through direct sales to builders, our Cabinets segment provides design, fabrication and installation services to single and multi-family homebuilders, remodelers and consumers under the brand names Armstrong<sup>®</sup> and Bruce<sup>®</sup>. All of Cabinets’ sales are in the U.S.

*Unallocated Corporate* – includes assets, liabilities, income and expenses that have not been allocated to the business units. Balance sheet items classified as Unallocated Corporate are primarily deferred income tax assets, cash and cash equivalents, the Armstrong brand name and the U.S. prepaid pension cost/liability. Expenses for our corporate departments and certain benefit plans are allocated to the reportable segments based on known metrics, such as time reporting, headcount, square-footage or net sales. The remaining items, which cannot be attributed to the reportable segments without a high degree of generalization, are reported in Unallocated Corporate.

The following chart illustrates the breakdown of our consolidated net sales for the year ended December 31, 2008 by segment:



See Note 4 to the Consolidated Financial Statements and Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K for additional financial information on our reportable segments.

**Markets**

The major markets in which we compete are:

*North American Residential.* Approximately 40% of our total consolidated net sales are for North American residential use. Our Resilient Flooring, Wood Flooring, Building Products and Cabinets segments sell products for use in the home. Homeowners have a multitude of finishing solution options for every room in their house. For flooring, they can choose from our vinyl and wood products, for which we are North America's largest provider, or from our laminate and ceramic products. We compete directly with other domestic and international suppliers of these products. Our flooring products also compete with carpet, which we do not offer. Our ceiling products compete against mineral fiber and fiberglass products from other manufacturers, as well as drywall. In the kitchen and bath areas, we compete with thousands of other cabinet manufacturers that include large diversified corporations as well as small local craftsmen.

Our products are used in new home construction and existing home renovation work. Industry estimates are that existing home renovation (also known as replacement / remodel) work represents approximately two-thirds of the total North American residential market opportunity. Key U.S. statistics that indicate market opportunity include existing home sales (a key indicator for renovation opportunity), housing starts, housing completions, interest rates and consumer confidence. For our Resilient Flooring and Wood Flooring products, we believe there is some longer-term correlation between these statistics and our revenue, after reflecting a lag period between change in construction activity and our operating results of several months. However, we believe that consumers' preferences for product type, style, color, availability and affordability also significantly impact our revenue. Further, changes in inventory levels and product focus at national home centers, which are our largest customers, can also significantly

impact our revenue. Sales of our ceiling products for residential use appear to follow the trend of existing home sales, with a several month lag period between change in existing home sales and our related operating results.

*North American Commercial.* Approximately 30% of our total consolidated net sales are for North American commercial use. Many of our products, primarily ceilings and Resilient Flooring, are used in commercial and institutional buildings. Our revenue opportunities come from new construction as well as renovation of existing buildings. Renovation work is estimated to represent approximately three-fourths of the total North American commercial market opportunity. Most of our revenue comes from four major segments of commercial building – office, education, retail and healthcare. We monitor U.S. construction starts (an indicator of U.S. monthly construction activity that provides us a reasonable indication of upcoming opportunity) and follow new projects. We have found that our revenue from new construction can lag behind construction starts by as much as one year. We also monitor office vacancy rates, GDP and general employment levels, which can indicate movement in renovation and new construction opportunities. We believe that these statistics, taking into account the time-lag effect, provide a reasonable indication of our future revenue opportunity from commercial renovation and new construction.

*Outside of North America.* The geographies outside of North America account for about 30% of our total consolidated net sales. Most of our revenues generated outside of North America are in Europe and are commercial in nature. For the countries in which we have significant revenue, we monitor various national statistics (such as GDP) as well as known new projects. Revenues come primarily from new construction and renovation work.

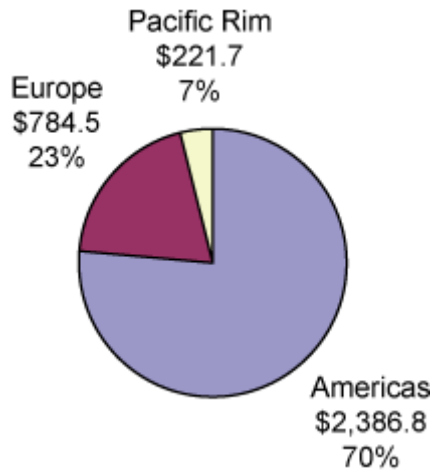
The following table provides an estimate of our segments' 2008 net sales, by major markets.

(Estimated percentages of individual segment's sales)	North American Residential	North American Commercial	Outside of North America	Total
Resilient Flooring	30%	35%	35%	100%
Wood Flooring	95%	5%	—	100%
Building Products	10%	50%	40%	100%
Cabinets	100%	—	—	100%

## **Geographic Areas**

We sell our products in more than 80 countries. Approximately 70% of our 2008 revenue was derived from sales in the Americas, the vast majority of which came in the United States and Canada. The following chart illustrates the breakdown of our consolidated net sales for the year ended December 31, 2008 by region, based on where the sale was made:

**2008 Consolidated Net Sales by Geography**  
(in millions)



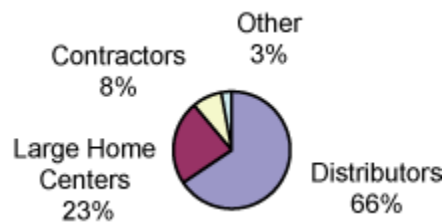
See Note 4 to the Consolidated Financial Statements and Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K for financial information by geographic areas.

## **Customers**

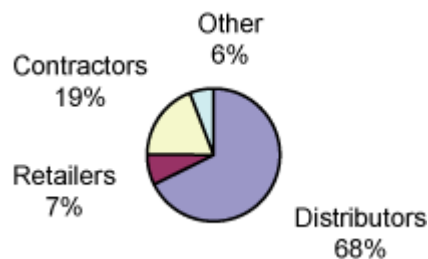
We use our reputation, capabilities, service and brand recognition to develop long-standing relationships with our customers. We principally sell products through building materials distributors, who re-sell our products to retailers, builders, contractors, installers and others. In the commercial sector, we also sell to several contractors and to subcontractors' alliances. In the North American retail channel, which sells to end-users in the residential and light commercial segments, we have important relationships with national home centers such as The Home Depot, Inc. and Lowe's Companies, Inc. In the North American residential sector, we have important relationships with major homebuilders and buying groups.

The following charts illustrate the estimated breakdown of our 2008 consolidated net sales geographically by distribution channel:

**2008 Americas Sale by Customer Type**



**2008 Non-Americas Sales by Customer Type**



Net sales to The Home Depot, Inc. were \$364.1 million in 2006, which was in excess of 10% of our consolidated net sales for that year. Net sales to The Home Depot were less than 10% of consolidated net sales in 2008 and 2007. Net sales to The Home Depot were recorded in our Resilient Flooring, Wood Flooring and Building Products segments. No other customers accounted for 10% or more of our total consolidated net sales.

**Product Array and Impact on Performance**

Each of our businesses offers a wide assortment of products that are differentiated by style/design and by performance attributes. Pricing for products within the assortment vary according to the level of value they provide. Changes in the relative quantity of products purchased at the different value points can impact year-to-year comparisons of net sales and operating income. Where significant, we discuss the impact of these relative changes as “product mix,” “customer mix” or “geographic mix” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-K.

**Competition**

There is strong competition in all of our businesses. Principal attributes of competition include product performance, product styling, service and price. Competition in North America comes from both domestic and international manufacturers. Additionally, some of our products compete with alternative products or finishing solutions. Our resilient, laminate and wood flooring products compete with carpet products, and our ceiling products compete with drywall and exposed structure (also known as open plenum). There is excess industry capacity for certain products in some geographies, which tends to increase price competition. The following companies are our primary competitors:

Flooring segments – Amtico International, Inc., Beaulieu International Group, N.V., Congoleum Corporation, Faus, Inc., Forbo Holding AG, Gerflor Group, Interface, Inc., IVC Group, Krono Holding AG, Mannington Mills, Inc., Mohawk Industries, Inc., Pfleiderer AG, Shaw Industries, Inc., Tarkett AG and Wilsonart International.

Building Products – CertainTeed, Chicago Metallic Corporation, Georgia-Pacific Corporation, Knauf AMF GmbH & Co. KG, Lafarge SA, Odenwald Faserplattenwerk GmbH, Rockfon A/S, Saint-Gobain and USG Corporation.

Cabinets – American Woodmark Corporation, Fortune Brands, Inc. and Masco Corporation.

**Raw Materials**

Raw materials essential to our businesses are purchased worldwide in the ordinary course of business from numerous suppliers. The principal raw materials used in each business include the following:

Business	Principal Raw Materials
Resilient Flooring	Polyvinylchloride (“PVC”) resins and films, plasticizers, backings, limestone, pigments, linseed oil, inks and stabilizers
Wood Flooring	Hardwood lumber, veneer, coatings and stains
Building Products	Mineral fibers, perlite, waste paper, clays, starches and steel used in the production of metal ceilings and for our joint venture’s manufacturing of ceiling grid
Cabinets	Lumber, veneer, plywood, particleboard and components, such as doors and hardware

We also purchase significant amounts of packaging materials and consume substantial amounts of energy, such as electricity and natural gas, and water.

In general, adequate supplies of raw materials are available to all of our businesses. However, availability can change for a number of reasons, including environmental conditions, laws and regulations, shifts in demand by other industries competing for the same materials, transportation disruptions and/or business decisions made by, or events that affect, our suppliers. There is no assurance that a significant shortage of raw materials will not occur.

Prices for certain high usage raw materials can fluctuate dramatically. Cost increases for these materials can have a significant adverse impact on our manufacturing costs. Given the competitiveness of our markets, we may not be able to recover the increased manufacturing costs through increasing selling prices to our customers.

## **Sourced Products**

Some of the products that we sell are sourced from third parties. The primary sourced products include laminate, wood flooring, vinyl sheet and tile and ceramic products, specialized ceiling products, and installation-related products and accessories for some of our manufactured products. We purchase some of our sourced products from suppliers that are located outside of the U.S., primarily from Asia and Europe. Sales of sourced products represented approximately 10% to 15% of our total consolidated revenue in 2008, 2007 and 2006.

In general, we believe we have adequate supplies of sourced products. However, we cannot guarantee that a significant shortage will not occur.


## **Hedging**

We use financial instruments to hedge the following exposures: sourced product purchases denominated in foreign currency, cross-currency intercompany loans and energy. We use derivative financial instruments as risk management tools, not for speculative trading purposes. See Item 7A. Quantitative and Qualitative Disclosures About Market Risk and Note 21 to the Consolidated Financial Statements of this Form 10-K for more information.

## **Patent and Intellectual Property Rights**

Patent protection is important to our business in the U.S. and other markets. Our competitive position has been enhanced by U.S. and foreign patents on products and processes developed or perfected within Armstrong or obtained through acquisitions and licenses. In addition, we benefit from our trade secrets for certain products and processes.

Patent protection extends for varying periods according to the date of patent filing or grant and the legal term of a patent in the various countries where patent protection is obtained. The actual protection afforded by a patent, which can vary from country to country, depends upon the type of patent, the scope of its coverage, and the availability of legal remedies. Although we consider that, in the aggregate, our patents, licenses and trade secrets constitute a valuable asset of material importance to our business, we do not regard any of our businesses as being materially dependent upon any single patent or trade secret, or any group of related patents or trade secrets.

Certain of our trademarks, including without limitation, house marks  , Armstrong<sup>®</sup>, Bruce<sup>®</sup>, Hartco<sup>®</sup>, Robbins<sup>®</sup>, Timberland<sup>®</sup>, Capella<sup>®</sup>, HomerWood<sup>®</sup> and DLW<sup>™</sup>, and product line marks Allwood<sup>™</sup>, Arteffects<sup>®</sup>, Axiom<sup>®</sup>, Capz<sup>™</sup>, Ceramaguard<sup>®</sup>, Cirrus<sup>®</sup>, Corlon<sup>®</sup>, Cortega<sup>®</sup>, CushionStep<sup>™</sup>, Designer Solarian<sup>®</sup>, Dune<sup>™</sup>, Excelon<sup>®</sup>, Fine Fissured<sup>™</sup>, Fundamentals<sup>®</sup>, Infusions<sup>®</sup>, Medintech<sup>®</sup>, Metalworks<sup>™</sup>, Natural Creations<sup>®</sup>, Natural Inspirations<sup>®</sup>, Nature's Gallery<sup>®</sup>, Optima<sup>®</sup>, Rhinofloor<sup>®</sup>, Sahara<sup>™</sup>, Scala<sup>®</sup>, Second Look<sup>®</sup>, Solarian<sup>®</sup>, SoundScapes<sup>®</sup>, StrataMax<sup>®</sup>, Techzone<sup>™</sup>, T. Morton<sup>™</sup>, ToughGuard<sup>®</sup> and Ultima<sup>®</sup>, Woodworks<sup>®</sup> are important to our business because of their significant brand name recognition. Trademark protection continues in some countries as long as the mark is used, and continues in other countries as long as the mark is registered. Registrations are generally for fixed, but renewable, terms.

## **Employees**

As of December 31, 2008, we had approximately 12,200 full-time and part-time employees worldwide, with approximately 8,400 employees located in the United States. Approximately 7,900 of the 12,200 are production and maintenance employees, of whom approximately 5,800 are located in the U.S. Approximately 63% of the production and maintenance employees in the U.S. are represented by labor unions. This percentage includes all production and maintenance employees at our plants and warehouses where labor unions exist. Outside the U.S., most of our production employees are covered by either industry-sponsored and/or state-sponsored collective bargaining mechanisms.

## **Research & Development**

Research and development (“R&D”) activities are important and necessary in helping us improve our products’ competitiveness. Principal R&D functions include the development and improvement of products and manufacturing processes. We spent \$38.8 million in 2008, \$44.0 million in 2007 and \$43.9 million in 2006 on R&D activities worldwide.

## **Environmental Matters**

Most of our manufacturing and certain of our research facilities are affected by various federal, state and local environmental requirements relating to the discharge of materials or the protection of the environment. We make expenditures necessary for compliance with applicable environmental requirements at each of our operating facilities.

We are actively involved in proceedings under the Comprehensive Environmental Response, Compensation and Liability Act (“CERCLA”), and similar state “Superfund” laws at four off-site locations. We have also been investigating and/or remediating environmental contamination allegedly resulting from past industrial activity at five domestic and five international current or former plant sites. Certain of AWI’s environmental liabilities were discharged through its Chapter 11 Case while others were not. Those environmental obligations that AWI has with respect to property that it owns or operates or for which a non-debtor subsidiary is liable were unaffected by the Chapter 11 Case. Therefore, AWI and its subsidiaries are required to continue meeting their ongoing environmental compliance obligations at such properties.

Liabilities of \$6.5 million and \$7.0 million at December 31, 2008 and December 31, 2007, respectively, were for potential environmental liabilities that we consider probable and for which a reasonable estimate of the probable liability could be made. See Note 32 to the Consolidated Financial Statements of this Form 10-K for more information.

## **ITEM 1A. RISK FACTORS**

As noted in the introductory section titled, “Uncertainties Affecting Forward-Looking Statements” above, our business, operations and financial condition are subject to various risks. These risks should be taken into account in evaluating any investment decision involving Armstrong. It is not possible to predict or identify all factors that could cause actual results to differ materially from expected and historical results. The following discussion is a summary of what we believe to be our most significant risk factors. These and other factors could cause our actual results to differ materially from those in forward-looking statements made in this report.

We try to reduce both the likelihood that these risks will affect our businesses and their potential impact. But, no matter how accurate our foresight, how well we evaluate risks, and how effective we are at mitigating them, it is still possible that one of these problems or some other issue could have serious consequences for us, up to and including a materially adverse effect. See related discussions in this document and our other SEC filings for more details and subsequent disclosures.

**Our business is dependent on construction activity. Downturns in construction activity and global economic conditions, such as weak consumer confidence and weak credit markets, adversely affect our business and our profitability.**

Our businesses have greater sales opportunities when construction activity is strong and, conversely, have fewer opportunities when such activity declines. Construction activity tends to increase when economies are strong, interest rates are favorable, government spending is strong, and consumers are confident. When the economy is weak and access to credit is limited, customers, distributors and suppliers are at heightened risk of defaulting on their obligations. Since most of our sales are in the U.S., its economy is the most important for our business, but conditions in Europe, Canada and Asia also are significant. A prolonged economic downturn would exacerbate the adverse effect on our business and profitability.



**We require a significant amount of liquidity to fund our operations.**

Our liquidity needs vary throughout the year. There are no significant debt maturities until 2011 and 2013 under our existing senior credit facility. We believe that cash on hand and generated from operations will be adequate to address our foreseeable liquidity needs. If future operating performance declines significantly, we cannot assure that our business will generate sufficient cash flow from operations to fund our needs or to remain in compliance with our debt covenants. In addition, we received a very substantial federal income tax refund in 2007. The tax year in question is still being audited by the IRS. If we were required to repay a substantial portion of the refund, our liquidity position would be adversely affected.

**Our markets are highly competitive. Competition can reduce demand for our products or cause us to lower prices. Failure to compete effectively by meeting consumer preferences and maintaining market share would adversely affect our results.**

Our customers consider our products' performance, product styling, customer service and price when deciding whether to purchase our products. Shifting consumer preference in our highly competitive markets, e.g. from residential vinyl products to other flooring products, styling preferences or inability to offer new competitive performance features could hurt our sales. For certain products, there is excess industry capacity in several geographic markets, which tends to increase price competition, as does competition from overseas competitors with lower cost structures.

**If the availability of raw materials and energy decreases, or the costs increase, and we are unable to pass along increased costs, our operating results could be adversely affected.**

The cost and availability of raw materials, packaging materials, energy and sourced products are critical to our operations. For example, we use substantial quantities of natural gas, petroleum-based raw materials, hardwood lumber and mineral fiber in our manufacturing operations. The cost of some items has been volatile in recent years and availability has sometimes been tight. We source some materials from a limited number of suppliers, which, among other things, increases the risk of unavailability. Limited availability could cause us to reformulate products or to limit our production. The impact of increased costs is greatest where our ability to pass along increased costs through price increases on our products is limited, whether due to competitive pressures or other factors.

**Reduction in sales to key customers could have a material adverse effect on our revenues and profits.**

Some of our businesses are dependent on a few key customers such as The Home Depot, Inc. and Lowe's Companies, Inc. The loss of sales to one of these major customers, or changes in our business relationship with them, could hurt both our revenues and profits.

**Changes in the political, regulatory and business environments of our international markets, including changes in trade regulations and currency exchange fluctuations, could have an adverse effect on our business.**

A significant portion of our products move in international trade, particularly among the U.S., Canada, Europe and Asia. Also, approximately 30% of our annual revenues are from operations outside the U.S. Our international trade is subject to currency exchange fluctuations, trade regulations, import duties, logistics costs and delays and other related risks. They are also subject to variable tax rates, credit risks in emerging markets, political risks, uncertain legal systems, restrictions on repatriating profits to the U.S., and loss of sales to local competitors following currency devaluations in countries where we import products for sale.

**Capital investments and restructuring actions may not achieve expected savings in our operating costs.**

We look for ways to make our operations more efficient and effective. We reduce, move and expand our plants and operations as needed. Each action generally involves substantial planning and capital investment. We can err in planning and executing our actions, which could hurt our customer service and cause unplanned costs.

**Labor disputes or work stoppages could hurt production and reduce sales and profits.**

Most of our manufacturing employees are represented by unions and are covered by collective bargaining or similar agreements that must be periodically renegotiated. Although we anticipate that we will reach new contracts as current ones expire, our negotiations may result in a significant increase in our costs. Failure to reach new contracts could lead to work stoppages, which could hurt production, revenues, profits and customer relations.

**Adverse judgments in regulatory actions, product claims and other litigation could be costly. Insurance coverage may not be available or adequate in all circumstances.**

While we strive to ensure that our products comply with applicable government regulatory standards and internal requirements, and that our products perform effectively and safely, customers from time to time could claim that our products do not meet contractual requirements, and users could be harmed by use or misuse of our products. This could give rise to breach of contract, warranty or recall claims, or claims for negligence, product liability, strict liability, personal injury or property damage. The building materials industry has been subject to claims relating to silicates, mold, PVC, formaldehyde, toxic fumes, fire-retardant properties and other issues, as well as for incidents of catastrophic loss, such as building fires. Product liability insurance coverage may not be available or adequate in all circumstances. In addition, claims may arise related to patent infringement, environmental liabilities, distributor terminations, commercial contracts, antitrust or competition law, employment law and employee benefits issues, and other regulatory matters. While we have in place processes and policies to mitigate these risks and to investigate and address such claims as they arise, we cannot predict the costs to defend or resolve such claims.

**Our principal shareholder could significantly influence our business and our affairs.**

The Armstrong World Industries, Inc. Asbestos Personal Injury Settlement Trust, formed in 2006 as part of AWI's emergence from bankruptcy, holds approximately 65% of outstanding shares. Such a large ownership could result in below average equity market liquidity and affect matters which require approval by our shareholders.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

Our world headquarters are in Lancaster, Pennsylvania. We own a 100-acre, multi-building campus comprising the site of our corporate headquarters, most operational headquarters, our U.S. R&D operations and marketing, and customer service headquarters. Altogether, our headquarters' operations occupy approximately one million square feet of floor space.

We produce and market Armstrong products and services throughout the world, operating 40 manufacturing plants in 10 countries as of December 31, 2008. Three of our plants are leased and the remaining 37 are owned. We have 25 plants located throughout the United States. In addition, we have an interest through our WAVE joint venture in seven additional plants in five countries.

<u>Business Segment</u>	<u>Number of Plants</u>	<u>Location of Principal Facilities</u>
Resilient Flooring	13	U.S. (California, Illinois, Mississippi, Oklahoma, Pennsylvania), Australia, Canada, Germany, Sweden and the U.K.
Wood Flooring	11	U.S. (Arkansas, Kentucky, Mississippi, Missouri, North Carolina, Pennsylvania, Tennessee, Texas, West Virginia)
Building Products	14	U.S. (Alabama, Florida, Georgia, Oregon, Pennsylvania), China, France, Germany and the U.K.
Cabinets	2	U.S. (Nebraska and Pennsylvania)

As part of our ongoing cost reduction efforts, in February 2009 we announced the idling of a Resilient Flooring plant in Canada and a Wood Flooring plant in Mississippi. Both plants are expected to be idled in the second quarter of 2009.

Sales and administrative offices are leased and/or owned worldwide, and leased facilities are utilized to supplement our owned warehousing facilities.

Production capacity and the extent of utilization of our facilities are difficult to quantify with certainty. In any one facility, utilization of our capacity varies periodically depending upon demand for the product that is being manufactured. We believe our facilities are adequate and suitable to support the business. Additional incremental investments in plant facilities are made as appropriate to balance capacity with anticipated demand, improve quality and service, and reduce costs.

**ITEM 3. LEGAL PROCEEDINGS**

See Note 32 to the Consolidated Financial Statements, which is incorporated herein by reference, for a full description of our legal proceedings.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted to a vote of stockholders during the fourth quarter of 2008.

## **ITEM 4A. EXECUTIVE OFFICERS OF THE COMPANY**

### **Executive Officer Information**

The following information is current as of February 26, 2009. Each executive officer serves a one-year term until reelected or until his earlier death, resignation, retirement or removal.

#### **Michael D. Lockhart**

Age 59 – Chairman of the Board, President and Chief Executive Officer since December 2002. Chairman of the Board and President since March 2001. Chairman and Chief Executive Officer of our former holding company from August 2000 – December 2007. Mr. Lockhart previously served as Chairman and Chief Executive Officer of General Signal (a diversified manufacturer) headquartered in Stamford, Connecticut from September 1995 until it was acquired in October 1998. He joined General Signal as President and Chief Operating Officer in September 1994. From 1981 until 1994, Mr. Lockhart worked for General Electric in various executive capacities in the GE Credit Corporation (now GE Capital), GE Transportation Systems and GE Aircraft Engines. Mr. Lockhart is a member of the Board of Directors of the Norfolk Southern Corporation and a member of the Business Council for the Graduate School of Business at the University of Chicago.

#### **F. Nicholas Grasberger, III**

Age 45 – Senior Vice President and Chief Financial Officer since January 2005. Previously Vice President and Chief Financial Officer of Kennametal, Inc. (a manufacturer of cutting tools and wear parts) August 2000 – December 2004. Formerly employed at H. J. Heinz (a global U.S. based food company) for eleven years, his last title being Treasurer.

#### **Donald A. McCunniff**

Age 51 – Senior Vice President, Human Resources since March 2006. Previously Vice President Human Resources, Corporate, Honeywell International (a global diversified technology and manufacturing company). Joined Honeywell in 1995 and served in various senior level Human Resources positions in Defense and Space, Electronics, Process Automation, and Aircraft Landing Systems.

#### **Frank J. Ready**

Age 47 – Executive Vice President and Chief Executive Officer North American Flooring Products since April 2008. Previously, President and Chief Executive Officer, North American Flooring Operations, June 2004 – April 2008. Previously Senior Vice President, Sales and Marketing, July 2003 – June 2004; Senior Vice President, Operations, December 2002 – July 2003; Senior Vice President, Marketing, June 2000 – December 2002.

#### **Stephen J. Senkowski**

Age 57 – Executive Vice President and Chief Executive Officer, Armstrong Building Products & Asia-Pacific Operations since April 2008. Previously, Executive Vice President since 2004 and President and Chief Executive Officer, Armstrong Building Products, October 2000 – April 2008; Senior Vice President, Americas, Building Products Operations, April 2000 – October 2000; President/Chief Executive Officer, WAVE (the Company's ceiling grid joint venture) July 1997 – April 2000; Vice President, Innovation Process, Building Products Operations 1994 – July 1997.

#### **Stephen F. McNamara**

Age 42 – Vice President and Controller since July 2008. Previously, Director, Internal Audit, November 2005 – July 2008; Assistant Controller, October 2001 – November 2005; Manager of External Reporting, May 1999 – October 2001. Prior to that he was Assistant Controller with Hunt Corporation (a former international art and office supply company).

**Jeffrey D. Nickel**

Age 46 – Senior Vice President, Secretary and General Counsel since August 2008. Previously Deputy General Counsel – Business and Commercial Law, September 2001 – July 2008. Prior to that he worked for Dow Corning Corporation (specialty chemical company), December 1992 – September 2001, his last title being senior attorney.

## PART II

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

Following AWI's emergence from Chapter 11, AWI's new common shares began trading on the New York Stock Exchange on October 10, 2006 under the ticker symbol "AWI". As of February 19, 2009, there were approximately 650 holders of record of AWI's Common Stock.

	First	Second	Third	Fourth	Total Year
2008					
Price range of common stock—high	\$ 40.98	\$ 39.44	\$ 40.19	\$ 28.94	\$ 40.98
Price range of common stock—low	\$ 26.25	\$ 28.92	\$ 27.10	\$ 13.79	\$ 13.79
2007					
Price range of common stock—high	\$ 56.72	\$ 57.48	\$ 52.47	\$ 44.28	\$ 57.48
Price range of common stock—low	\$ 41.55	\$ 49.85	\$ 35.04	\$ 38.00	\$ 35.04

The above figures represent the high and low intra-day sale prices for our common stock as reported by the New York Stock Exchange.

On February 25, 2008, our Board of Directors declared a special cash dividend of \$4.50 per common share, payable on March 31, 2008, to shareholders of record on March 11, 2008. This special cash dividend resulted in an aggregate cash payment to our shareholders of \$256.4 million. There were no dividends declared or paid during 2007.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share <sup>1</sup>	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>2</sup>	Maximum Number of Shares that may yet be Purchased under the Plans or Programs
October 1–31, 2008	29,025	\$ 28.55	—	—
November 1–30, 2008	—	—	—	—
December 1–31, 2008	8,400	\$ 20.92	—	—
Total	37,425		N/A	N/A

<sup>1</sup> Shares reacquired through the withholding of shares to pay employee tax obligations upon the vesting of restricted shares previously granted under the 2006 Long Term Incentive Plan.

<sup>2</sup> The Company does not have a share buy-back program.

**ITEM 6. SELECTED FINANCIAL DATA**

	Successor Company			Predecessor Company		
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006 <sup>(1)</sup>	Year 2005	Year 2004
<b>(Dollars in millions except for per-share data)</b>						
<b>Income statement data</b>						
Net sales	\$ 3,393.0	\$ 3,549.7	\$ 817.3	\$ 2,608.6	\$ 3,326.6	\$ 3,279.1
Cost of goods sold	2,632.0	2,687.5	660.9	2,030.2	2,654.0	2,655.6
Selling, general and administrative expenses	579.9	611.3	143.5	415.5	587.8	566.5
Goodwill and intangibles impairment	25.4	—	—	—	—	108.4
Restructuring charges, net	0.8	0.2	1.7	10.0	23.0	17.9
Equity (earnings) from joint ventures	(56.0)	(46.0)	(5.3)	(41.4)	(39.3)	(31.6)
Operating income (loss)	210.9	296.7	16.5	194.3	101.1	(37.7)
Interest expense	30.8	55.0	13.4	5.2	7.7	7.9
Other non-operating expense	1.3	1.4	0.3	1.0	1.5	3.1
Other non-operating (income)	(10.6)	(18.2)	(4.3)	(7.2)	(11.8)	(6.4)
Chapter 11 reorganization (income) costs, net	—	(0.7)	—	(1,955.5)	(1.2)	6.9
Income tax expense (benefit)	109.0	106.4	3.8	726.6	(1.2)	21.4
Earnings (loss) from continuing operations	80.4	152.8	3.3	1,424.2	106.1	(70.6)
Per common share – basic (a)	\$ 1.43	\$ 2.73	\$ 0.06	n/a	n/a	n/a
Per common share – diluted (a)	\$ 1.42	\$ 2.69	\$ 0.06	n/a	n/a	n/a
Earnings (loss) from discontinued operations	0.6	(7.5)	(1.1)	(68.4)	5.0	(9.1)
Net earnings (loss)	\$ 81.0	\$ 145.3	\$ 2.2	\$ 1,355.8	\$ 111.1	\$ (79.7)
Per common share – basic (a)	\$ 1.44	\$ 2.59	\$ 0.04	n/a	n/a	n/a
Per common share – diluted (a)	\$ 1.43	\$ 2.56	\$ 0.04	n/a	n/a	n/a
Dividends declared per share of common stock	\$ 4.50	n/a	n/a	n/a	n/a	n/a
Average number of common shares outstanding (in millions)	57.1	56.6	55.0	n/a	n/a	n/a
Average number of employees	12,500	13,500	14,500	14,700	14,900	15,400
<b>Balance sheet data (end of period)</b>						
Working capital	\$ 876.1	\$ 1,003.7	\$ 854.6		\$ 1,128.0	\$ 985.8
Total assets	3,351.8	4,639.4	4,152.7		4,602.1	4,604.9
Liabilities subject to compromise	—	—	1.3		4,869.4	4,870.9
Net long-term debt (b)	454.8	485.8	801.5		21.5	29.2
Shareholders' equity (deficit)	1,744.3	2,437.2	2,164.5		(1,319.9)	(1,425.3)

(1) Reflects the effects of the Plan of Reorganization and fresh-start reporting. See Note 3 to the Consolidated Financial Statements.

**Notes:**

- (a) See definition of basic and diluted earnings per share in Note 2 of the Consolidated Financial Statements. The common stock of the Predecessor Company was not publicly traded.
- (b) Net long-term debt excludes debt subject to compromise for 2005 and 2004.

Certain prior year amounts have been reclassified to conform to the current year presentation. See Note 2 to the Consolidated Financial Statements.

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

Armstrong World Industries, Inc. ("AWI") is a Pennsylvania corporation incorporated in 1891. When we refer to "we", "our" and "us" in this report, we are referring to AWI and its subsidiaries. References in this report to "reorganized Armstrong" are to AWI as it was reorganized under the Plan of Reorganization ("POR") on October 2, 2006, and its subsidiaries collectively. We use the term "AWI" when we are referring solely to Armstrong World Industries, Inc.

This discussion should be read in conjunction with the financial statements and the accompanying notes included elsewhere in this Form 10-K. This discussion contains forward-looking statements based on our current expectations, which are inherently subject to risks and uncertainties. Actual results and the timing of certain events may differ significantly from those referred to in such forward-looking statements. We undertake no obligation beyond what is required under applicable securities law to publicly update or revise any forward-looking statement to reflect current or future events or circumstances, including those set forth in the section entitled "Uncertainties Affecting Forward-Looking Statements" and elsewhere in this Form 10-K.

Financial performance metrics which exclude the translation effect of changes in foreign exchange rates are not in compliance with U.S. generally accepted accounting principles ("GAAP"). We believe that this information improves the comparability of business performance. We calculate the translation effect of foreign exchange rates by applying constant foreign exchange rates to the equivalent periods' reported foreign currency amounts. We believe that this non-GAAP metric provides a clearer picture of our operating performance. Furthermore, management evaluates the performance of the businesses excluding the effects of foreign exchange rates.

In connection with its emergence from bankruptcy on October 2, 2006 (the "Effective Date"), AWI adopted fresh-start reporting in accordance with AICPA Statement of Position 90-7, "Financial Reporting by Entities in Reorganization under the Bankruptcy Code" ("SOP 90-7"). Adopting fresh-start reporting has resulted in material adjustments to the historical carrying amount of reorganized Armstrong's assets and liabilities. See Note 3 to the Consolidated Financial Statements for more information. As a result, our post-emergence financial statements are not comparable to our pre-emergence financial statements. Despite the lack of comparability, we have combined the 2006 results of the Predecessor Company (which represent the first nine months of 2006 and include the impact of emergence) with the results of the Successor Company (which represent the last three months of 2006) to facilitate the year-to-year discussion of operating results in certain sections of this Form 10-K, including relevant portions of Management's Discussion and Analysis. The combined financial information for 2006 is merely cumulative and does not give pro forma effect to the Predecessor's results as if the consummation of the POR and the related fresh-start reporting and other adjustments had occurred at the beginning of the period presented. Combining pre-emergence and post-emergence results is not in accordance with GAAP.

We maintain a website at <http://www.armstrong.com>. Information contained on our website is not necessarily incorporated into this document. Annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, all amendments to those reports and other information about us are available free of charge through this website as soon as reasonably practicable after the reports are electronically filed with the Securities and Exchange Commission ("SEC"). These materials are also available from the SEC's website at [www.sec.gov](http://www.sec.gov).



Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

**OVERVIEW**

We are a leading global producer of flooring products and ceiling systems for use primarily in the construction and renovation of residential, commercial and institutional buildings. Through our United States ("U.S.") operations and U.S. and international subsidiaries, we design, manufacture and sell flooring products (primarily resilient and wood) and ceiling systems (primarily mineral fiber, fiberglass and metal) around the world. We also design, manufacture and sell kitchen and bathroom cabinets in the U.S. As of December 31, 2008 we operated 40 manufacturing plants in 10 countries, including 25 plants located throughout the U.S. Through WAVE, our joint venture with Worthington Industries, Inc., we also have an interest in seven additional plants in five countries that produce suspension system (grid) products for our ceiling systems.

We report our financial results through the following segments: Resilient Flooring, Wood Flooring, Building Products, Cabinets and Unallocated Corporate. See "Results of Operations" and "Reportable Segment Results" for additional financial information on our consolidated company and our segments.

Our consolidated net sales for 2008 were \$3.4 billion, approximately 4% less than consolidated net sales in 2007. Operating income was \$210.9 million in 2008, as compared to \$296.7 million in 2007. Continuing declines in domestic residential markets were exacerbated by increasing weakness in domestic and international commercial markets. The broad market weakness accelerated significantly in the last two months of the year. For the year, sales volume declines, input cost inflation and intangible asset impairments more than offset higher selling prices and lower manufacturing and selling, general and administrative ("SG&A") expenses.

- **Resilient Flooring** sales declined modestly. Volume declines in the Americas and Europe offset price and product mix improvements across geographies. Operating income declined significantly due to lower sales, inflation and cost reduction expenses.
- **Wood Flooring** sales continued to decline with weak new residential housing and renovation markets. Operating income declined significantly as the impact from lower sales and intangible asset impairments more than offset reduced manufacturing and SG&A expenses.
- **Building Products** again generated record sales and operating income despite significant slowing in the U.S. commercial markets toward the end of the year. Price and product mix improvements across geographies and volume growth in the Pacific Rim markets offset volume declines in the Americas and Europe. Operating income grew on higher sales and increased income from WAVE, despite significant cost inflation.
- **Cabinets** had significant declines in sales and operating income due to lower unit volume. Similar to Wood Flooring, the declines reflect a significant exposure to residential housing activity.
- **Corporate Unallocated** expense declined \$37.0 million due to lower incentive compensation expense and 2007 expenses related to our review of strategic alternatives and Chapter 11 related post-emergence expenses, which were not repeated in 2008.

During 2008, our cash and cash equivalents decreased by \$159.3 million, primarily due to a special cash dividend of \$256.4 million.

Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

**Factors Affecting Revenues**

For an estimate of our segments' 2008 net sales by major markets, see "Markets" in Item 1. Business of this Form 10-K.

*Markets.* We compete in building material markets around the world. The majority of our sales are in North America and Europe. During 2008, these markets experienced the following:

- According to the U.S. Census Bureau, in 2008, housing starts in the U.S. residential market declined 32.7% compared to 2007 to 0.90 million units. Housing completions in the U.S. decreased by 25.8% in 2008 with approximately 1.12 million units completed. The National Association of Realtors indicated that sales of existing homes decreased 13.7% to 4.90 million units in 2008 from a level of 5.67 million in 2007.

According to the U.S. Census Bureau, U.S. retail sales through building materials, garden equipment and supply stores (an indicator of home renovation activity) decreased 3.97% in 2008 compared 2007.

- According to the U.S. Census Bureau the rate of growth in the North American key commercial market, in nominal dollar terms, was 5.6% in 2008. Construction activity in the office, healthcare, retail and education segments increased 12.3%, 8.6%, -3.6% and 8.3%, respectively, in 2008, with the rate of growth in all segments being down from 2007 rates.
- Markets in both Western and Eastern European countries generally slowed over the course of the year, with most markets down year-over-year by the fourth quarter.
- Pacific Rim markets also generally began to slow toward the end of the year.

*Quality and Customer Service.* Our quality and customer service are critical components of our total value proposition. In 2008, we experienced no significant quality or customer service issues.

*Pricing Initiatives .* We periodically modify prices in response to changes in costs for raw materials and energy, and to market conditions and the competitive environment. The net impact of these pricing initiatives improved sales in 2008 compared to 2007.

The most significant of these pricing actions were:

- Resilient Flooring implemented price increases on selected products in March, July and October 2008.
- Wood Flooring had no significant pricing actions in 2008.
- Building Products announced price increases across geographies in each quarter of 2008 due to continuing cost inflation.
- Cabinets' only increase for the year was in February 2008.

In certain cases, realized price increases are less than the announced price increases because of competitive reactions and changing market conditions.

We estimate pricing actions increased our total consolidated net sales in 2008 compared to 2007 by approximately \$84 million.

Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

*Mix.* Each of our businesses offers a wide assortment of products that are differentiated by style/design and by performance attributes. Pricing for products within the assortment varies. Changes in the relative quantity of products purchased at the different price points can impact year-to-year comparisons of net sales and operating income. We estimate mix changes increased our total consolidated net sales in 2008 by approximately \$47 million when compared to 2007.

**Factors Affecting Operating Costs**

*Operating Expenses.* Our operating expenses consist of direct production costs (principally raw materials, labor and energy) and manufacturing overhead costs, costs to purchase sourced products and SG&A expenses.

Our largest individual raw material expenditures are for lumber and veneers, PVC resins and plasticizers. Natural gas is also a significant input cost. Fluctuations in the prices of these inputs are generally beyond our control and have a direct impact on our financial results. In 2008 the net impact of these input costs was approximately \$87 million higher than in the same period of the previous year.

*Intangible Asset Impairment.* During the fourth quarter of 2008, we recorded a non-cash impairment charge of \$25.4 million to reduce the carrying amount of our Wood Flooring trademarks to their estimated fair value. The fair value was negatively affected by lower expected future cash flows due to the decline in the U.S. residential housing market. See Note 12 to the Consolidated Financial Statements for more information regarding our intangible asset impairment charge.

*Cost Reduction Initiatives.* During 2008 we recorded \$20.0 million of charges (severance of \$17.7 million and accelerated depreciation of \$2.3 million) primarily related to organizational and manufacturing changes for our European resilient flooring business and the termination costs for certain corporate employees. The European organizational changes are due to the decision to consolidate and outsource several SG&A functions. The manufacturing changes primarily related to the decision to cease production of automotive carpeting and other specialized textile flooring products. These charges were recorded as part of cost of goods sold (\$7.3 million) and SG&A expense (\$12.7 million). We expect to incur approximately \$5 million of additional charges for severance and accelerated depreciation in 2009 for these initiatives.

During 2004, we implemented several significant manufacturing and organizational programs to improve our cost structure and enhance our competitive position. We incurred significant costs from 2004 through 2006 related to these initiatives. Our largest initiative involved ceasing production of certain products at our Resilient Flooring manufacturing plant in Lancaster, Pennsylvania, transferring production to other Resilient Flooring plants. All 2004 initiatives have been fully implemented, and we do not expect to incur additional expenses in future periods for these initiatives.

In 2006, we incurred \$30.1 million of charges (\$11.0 million in cost of goods sold, \$7.4 million in SG&A expenses and \$11.7 million in restructuring charges) to implement cost reduction initiatives, with \$27.4 million of these charges recorded in the Resilient Flooring segment. Cost of goods sold includes \$0.7 million of fixed asset impairments (incurred in the nine months ended September 30, 2006), \$0.3 million of accelerated depreciation (incurred in the nine months ended September 30, 2006) and \$10.0 million of other related costs in 2006 (\$0.6 million incurred in the three months ended December 31, 2006 and \$9.4 million incurred in the nine months ended September 30, 2006).

In 2006, we also recorded a gain of \$14.3 million from the sale of a warehouse which became available as a result of the Resilient Flooring cost reduction initiatives. This gain was recorded in SG&A expenses.

See Note 16 to the Consolidated Financial Statements for more information on restructuring charges.

Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

*On-going Cost Improvements.* In addition to the above-mentioned cost reduction programs we have an ongoing focus on continually improving our cost structure. As a result of these cost reduction initiatives and our on-going improvement efforts, we have realized significant reductions in our manufacturing conversion costs. Additional charges may be incurred in future periods for further cost reduction actions.

*Fresh Start Reporting.* In connection with its emergence from bankruptcy on October 2, 2006, AWI adopted fresh-start reporting. For administrative convenience, we selected September 30, 2006, following the close of business, as the date to adopt fresh-start reporting. See Note 3 to the Consolidated Financial Statements for more information.

Adopting fresh-start reporting resulted in material adjustments to the historical carrying amount of reorganized Armstrong's assets and liabilities. Certain of these adjustments impacted our statements of earnings for the periods following emergence, through changes in depreciation and amortization, costs for benefit plans, costs for hedging-related activity, inventory-related costs and WAVE's earnings. In 2006, fresh-start reporting impacted fourth quarter earnings. Fresh-start reporting impacted all periods in 2007, with the fourth quarter's impact being different than the first three quarters due to the revisions made to the fresh-start balance sheet based upon filing our federal income tax return in September 2007 (see Note 3 to the Consolidated Financial Statements for more information). Please see page 32 for the dollar impact of fresh-start reporting by operating expense type for each period.

*Review of Strategic Alternatives .* On February 15, 2007, we announced that we had initiated a review of our strategic alternatives. On February 29, 2008, we announced that we have completed the strategic review process after extensive evaluation of alternatives, including a possible sale of our individual businesses and the entire company. The Board of Directors concluded that it is in the best interest of Armstrong and its shareholders to continue to execute our strategic operating plan under our current structure as a publicly traded company. We incurred costs in conjunction with this review of \$1.2 million in the first quarter of 2008.

See also "Results of Operations" for further discussion of other significant items affecting operating costs.

### **Factors Affecting Cash Flows**

Typically, we generate cash in our operating activities. The amount of cash generated in a period is dependent on a number of factors, including the amount of operating profit generated, the amount of working capital (such as inventory, receivables and payables) required to operate our businesses and investments in property, plant & equipment and computer software ("PP&E").

During 2008, our cash and cash equivalents decreased by \$159.3 million, primarily due to a special cash dividend of \$256.4 million. Net cash from operating activities of \$214.2 million was partially offset by capital expenditures of \$95.0 million. During 2007, our cash and cash equivalents increased by \$250.5 million, as net cash from operating activities, including distributions from WAVE of \$117.5 million (which included special distributions of \$50.0 million) and net U.S. federal income tax refunds of \$209.1 million, more than offset \$300 million of voluntary debt principal prepayments and capital expenditures of \$102.6 million. We also received \$58.8 million in proceeds from a divestiture.

### **Employees**

As of December 31, 2008, we had approximately 12,200 full-time and part-time employees worldwide. This compares to approximately 12,900 employees as of December 31, 2007. The decline reflects headcount reductions, primarily in the wood flooring and cabinets segments.

During 2008, we negotiated eight collective bargaining agreements and none of our locations experienced work stoppages. Throughout 2009, collective bargaining agreements covering approximately 1,900 employees at five plants are scheduled to expire.

Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

As part of our ongoing cost reduction efforts, in February 2009 we announced layoffs at manufacturing facilities in North America impacting approximately 600 employees. The layoffs will occur in the first and second quarters of 2009.

**CRITICAL ACCOUNTING ESTIMATES**

In preparing our consolidated financial statements in accordance with U.S. generally accepted accounting principles ("GAAP"), we are required to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. We evaluate our estimates and assumptions on an on-going basis, using relevant information from inside and outside the Company. We believe that our estimates and assumptions are reasonable. However, actual results may differ from what was estimated and could have a significant impact on the financial statements.

We have identified the following as our critical accounting estimates. We have discussed these critical accounting estimates with our Audit Committee.

Fresh-Start Reporting and Reorganization Value – As part of our emergence from bankruptcy on October 2, 2006, we implemented fresh-start reporting in accordance with AICPA Statement of Position 90-7 ("SOP 90-7"), *Financial Reporting by Entities in Reorganization under the Bankruptcy Code*. Our assets, liabilities and equity were adjusted to fair value. In this regard, our Consolidated Financial Statements for periods subsequent to October 2, 2006 reflect a new basis of accounting and are not comparable to our historical consolidated financial statements for periods prior to October 2, 2006.

Under fresh-start reporting, a reorganization value was determined and allocated to our net assets based on their relative fair values in a manner similar to the accounting provisions applied to business combinations under Statement of Financial Accounting Standards No. 141, *Business Combinations*. The estimates and assumptions used to derive the reorganization value and allocation of value to balance sheet accounts were inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which were beyond our control. Modification to these assumptions could have significantly changed the reorganization value, and hence the resultant fair values of our assets and liabilities.

The adoption of fresh-start reporting had a material effect on our Consolidated Financial Statements and was based on assumptions that employed a high degree of judgment. See Notes 1 and 3 to the Consolidated Financial Statements for further information relative to our reorganization and the assumptions used to value reorganized Armstrong.

U.S. Pension Credit and Postretirement Benefit Costs – We maintain pension and postretirement plans throughout the world, with the most significant plans located in the U.S. The U.S. defined benefit pension plans were closed to new salaried and salaried production employees on January 1, 2005. We also froze benefits for certain non-production salaried employees effective February 28, 2006. Our defined benefit pension and postretirement benefit costs are developed from actuarial valuations. These valuations are calculated using a number of assumptions. Each assumption represents management's best estimate of the future. The assumptions that have the most significant impact on reported results are the discount rate, the estimated long-term return on plan assets and the estimated inflation in health care costs. These assumptions are generally updated annually. However, we also updated each of these assumptions and adopted Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans," as part of adopting fresh-start reporting in accordance with SOP 90-7.

The discount rate is used to determine retirement plan liabilities and to determine the interest cost component of net periodic pension and postretirement cost. Management utilizes the yield for Moody's AA-rated long-term corporate bonds as the primary basis for determining the discount rate. The duration of the securities underlying the Moody's AA-rated bond index is reasonably comparable to the duration of

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our retirement plan liabilities. As of December 31, 2008, we assumed a discount rate of 5.60% compared with a discount rate of 5.85% as of December 31, 2007 for the U.S. plans. This decrease is consistent with the decrease in U.S. corporate bond yields during the year. The effects of the decreased discount rate will be amortized into earnings as described below. A one-quarter percentage point decrease in the discount rate to 5.35% would increase 2009 operating income by \$0.7 million, as the resulting decrease in the interest cost component of the pension expense calculation would more than offset the increased service cost component. A one-quarter percentage point increase in the discount rate to 5.85% would reduce 2009 operating income by \$0.7 million.

We have two U.S. defined benefit pension plans, a qualified funded plan and a nonqualified unfunded plan. For the funded plan, the expected long-term return on plan assets represents a long-term view of the future estimated investment return on plan assets. This estimate is determined based on the target allocation of plan assets among asset classes and input from investment professionals on the expected performance of the equity and bond markets over 10 to 20 years. Over the last 10 years, the annualized return was approximately 4.3% compared to an average expected return of 8.5%. The expected long-term return on plan assets used in determining our 2008 U.S. pension credit was 8.0%. The actual return on plan assets achieved for 2008 was -23.9%. In accordance with GAAP, this deficit will be amortized into earnings as described below. We do not expect to make cash contributions to the qualified funded plan during 2009. We have assumed a return on plan assets during 2009 of 8.0%. A one-quarter percentage point increase or decrease in this assumption would increase or decrease 2009 operating income by approximately \$5.3 million. Contributions to the unfunded plan were \$3.2 million in 2008 and were made on a monthly basis to fund benefit payments. We estimate the contributions to be approximately \$3.3 million in 2009. See Note 19 to the Consolidated Financial Statements for more details.

The qualified funded defined benefit plan, which was previously overfunded, was underfunded in relation to its benefit obligations at December 31, 2008 primarily due to the impact of lower asset values in 2008.

The estimated inflation in health care costs represents a long-term view (5-10 years) of the expected inflation in our postretirement health care costs. We separately estimate expected health care cost increases for pre-65 retirees and post-65 retirees due to the influence of Medicare coverage at age 65, as illustrated below:

	Assumptions			Actual		
	Post 65	Pre 65	Overall	Post 65	Pre 65	Overall
2007	12.0%	11.5%	11.8%	(2)%	(3)%	(2)%
2008	11.0%	10.5%	10.8%	(5)%	12%	0%
2009	10.0%	9.5%	9.8%			

Actual health care cost increases were lower than expected in 2008, primarily due to favorable claims experience. In accordance with GAAP, the difference between the actual and expected health care costs is amortized into earnings as described below. As of December 31, 2008, health care cost increases are estimated to decrease by 1 percentage point per year until 2014, after which they are constant at 5%. A one percentage point increase in the assumed health care cost trend rate would reduce 2009 operating income by \$1.4 million, while a one percentage point decrease in the assumed health care cost trend rate would increase 2009 operating income by \$1.3 million. See Note 19 to the Consolidated Financial Statements for more details.

Actual results that differ from our various pension and postretirement plan estimates are captured as actuarial gains/losses. When certain thresholds are met, the gains and losses are amortized into future

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earnings over the expected remaining service period of plan participants, which is approximately nine years. Changes in assumptions could have significant effects on earnings in future years.

Impairments of Long-Lived Tangible and Intangible Assets – In connection with our adoption of fresh-start reporting upon emerging from Chapter 11, all long-lived tangible and intangible assets were adjusted to fair value. We periodically review significant tangible and definite-lived intangible assets for impairment under the guidelines of the Financial Accounting Standards Board Statement No. 144 – “Accounting for the Impairment or Disposal of Long-Lived Assets” (“FAS 144”). In accordance with this Statement, we review our businesses for indicators of impairment such as operating losses and/or negative cash flows. If an indication of impairment exists, we compare the carrying amount of the asset group to the estimated undiscounted future cash flows expected to be generated by the assets. The amount of impairment loss to be recognized is then measured by comparing the asset group's carrying amount to its fair value. The estimate of an asset group's fair value is based on discounted future cash flows expected to be generated by the asset group, or based on management's estimated exit price assuming the assets could be sold in an orderly transaction between willing parties. If the fair value is less than the carrying value of the asset group, we record an impairment charge equal to the difference between the fair value and carrying value of the asset group.

Our indefinite-lived intangibles are primarily trademarks and brand names, which are integral to our corporate identity and expected to contribute indefinitely to our corporate cash flows. Accordingly, they have been assigned an indefinite life. We perform annual impairment tests on these indefinite-lived intangibles under the guidelines of the Financial Accounting Standards Board Statement No. 142 – “Goodwill and Other Intangible Assets” (“FAS 142”). These assets undergo more frequent tests if an indication of possible impairment exists.

The principal assumptions utilized in our estimates for tangible and definite-lived intangible assets include operating profit adjusted for depreciation and amortization and discount rate. The principal assumptions utilized in our estimates for indefinite-lived intangible assets include revenue growth rate, discount rate and royalty rate. Revenue growth rate and operating profit assumptions are consistent with those utilized in our operating plan and long-term financial planning process. The discount rate assumption is calculated based upon an estimated weighted average cost of equity which reflects the overall level of inherent risk and the rate of return an investor would expect to achieve. Methodologies used for valuing our tangible and intangible assets did not change from prior periods.

The cash flow estimates used in applying FAS 142 and FAS 144 are based on management's analysis of information available at the time of the impairment test. Actual cash flows lower than the estimate could lead to significant future impairments. If subsequent testing indicates that new fair values have declined, the carrying values would be reduced and our future statements of income would be impacted.

During the fourth quarter of 2008, we recorded a non-cash impairment charge of \$25.4 million to reduce the carrying amount of our Wood Flooring trademarks to their estimated fair value based on the results of our annual impairment test. The fair value was negatively affected by lower expected future cash flows due to the decline in the U.S. residential housing market.

See Notes 10 and 12 to the Consolidated Financial Statements for further information.

Sales-related Accruals – We provide direct customer and end-user warranties for our products. These warranties cover manufacturing defects that would prevent the product from performing in line with its intended and marketed use. The terms of these warranties vary by product line and generally provide for the repair or replacement of the defective product. We collect and analyze warranty claims data with a focus on the historical amount of claims, the products involved, the amount of time between the warranty claims and the products' respective sales and the amount of current sales.

We also maintain numerous customer relationships that incorporate different sales incentive programs (primarily volume rebates and promotions). The rebates vary by customer and usually include tiered incentives based on the level of customers' purchases. Certain promotional allowances are also tied to

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customer purchase volumes. We estimate the amount of expected annual sales during the course of the year and use the projected sales amount to estimate the cost of the incentive programs. For sales incentive programs that are on the same calendar basis as our fiscal calendar, actual sales information is used in the year-end accruals.

While historical results have not differed materially from our estimated accruals, future experience related to these accruals could differ significantly from the estimated amounts during the year. If this occurs, we would adjust our accruals accordingly. Our sales-related accruals totaled \$64.5 million and \$79.7 million as of December 31, 2008 and 2007, respectively. We record the costs of these accruals as a reduction of gross sales.

**Income Taxes** – Our effective tax rate is primarily determined based on our pre-tax income and the statutory income tax rates in the jurisdictions in which we operate. The effective tax rate also reflects the tax impacts of items treated differently for tax purposes than for financial reporting purposes. Some of these differences are permanent, such as expenses that are not deductible in our tax returns, and some differences are temporary, reversing over time, such as depreciation expense. Deferred tax assets are also recorded for operating loss, capital loss and tax credit carryforwards. These temporary differences create deferred income tax assets and liabilities.

Deferred income tax assets and liabilities are recognized by applying enacted tax rates to temporary differences that exist as of the balance sheet date. We record valuation allowances to reduce our deferred income tax assets if it is more likely than not that some portion or all of the deferred income tax assets will not be realized. As of December 31, 2008, we have recorded valuation allowances totaling \$208.7 million for various state and foreign net operating loss, capital loss and foreign tax credit carryforwards. While we have considered future taxable income in assessing the need for the valuation allowances based on our best available projections, if these estimates and assumptions change in the future or if actual results differ from our projections, we may be required to adjust our valuation allowances accordingly. Such adjustment could be material to our Consolidated Financial Statements.

As further described in Note 17 to the Consolidated Financial Statements, our Consolidated Balance Sheet as of December 31, 2008 includes net deferred income tax assets of \$691.9 million. Included in these amounts are deferred federal and state income tax assets of \$357.6 million and \$62.1 million, respectively, relating to federal and state net operating loss carryforwards. These net operating losses arose primarily as a result of the amounts paid to the Asbestos PI Trust in 2006. We have concluded that all but \$23.8 million of these income tax benefits are more likely than not to be realized in the future.

Inherent in determining our effective tax rate are judgments regarding business plans and expectations about future operations. These judgments include the amount and geographic mix of future taxable income, limitations on usage of net operating loss carryforwards after emergence from bankruptcy, potential tax law changes, the impact of ongoing or potential tax audits, earnings repatriation plans and other future tax consequences.

In accordance with the requirements for fresh-start reporting pursuant to SOP 90-7, we adopted FASB Interpretation No. 48 ("FIN 48"), Accounting for Uncertainty in Income Taxes, effective as of October 2, 2006. We establish reserves for tax positions that management believes are supportable, but are potentially subject to successful challenge by the applicable taxing authorities. We review these tax uncertainties in light of the changing facts and circumstances and adjust them when warranted. We have several tax audits in process in various jurisdictions.

**ACCOUNTING PRONOUNCEMENTS EFFECTIVE IN FUTURE PERIODS**

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 157 "Fair Value Measurements" ("FAS 157"), which establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. FAS 157 was generally effective for fiscal years beginning after November 15, 2007. However the effective date for certain non-financial assets and liabilities was deferred to fiscal



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years beginning after November 15, 2008. We do not expect any material impact from adopting the remaining portions of FAS 157.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 Revised 2007, "Business Combinations" ("FAS 141R"). FAS 141R revises the original FAS 141, while retaining the underlying concept that all business combinations be accounted for at fair value. However, FAS 141R changes the methodology of applying this concept in that acquisition costs will generally be expensed as incurred, non-controlling interests will be valued at fair value, in-process research and development will be recorded at fair value as an indefinite-lived intangible, restructuring costs associated with a business combination will generally be expensed subsequent to the acquisition and changes in deferred income tax asset allowances after the acquisition date generally will affect income tax expense. This pronouncement applies prospectively to all business combinations whose acquisition dates are on or after the beginning of the first annual period subsequent to December 15, 2008. Additionally, under FAS 141R certain future adjustments to deferred income tax valuation allowances and uncertain tax positions recognized upon our emergence from bankruptcy will impact future earnings.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, "Non-controlling Interests in Consolidated Financial Statements – an amendment of ARB No. 51" ("FAS 160"). FAS 160 requires the recognition of a non-controlling interest (formerly known as a "minority interest") as equity in the consolidated financial statements and separate from the parent's equity. The amount of net income attributable to the non-controlling interest will be included in consolidated net income on the face of the income statement. It also amends certain of ARB 51's consolidation procedures for consistency with the requirements of FAS 141R. This pronouncement is effective for fiscal years, and all interim periods within those fiscal years, beginning after December 15, 2008. Early adoption is not permitted. We do not expect any material impact from adopting FAS 160.

In November 2008 the FASB issued Emerging Issues Task Force No. 08-6 ("EITF 08-6"), "Equity Method Investment Accounting Considerations". EITF 08-6 discusses the accounting for contingent consideration agreements of an equity method investment and the requirement for the investor to recognize its share of any impairment charges recorded by the investee. EITF 08-6 requires the investor to record share issuances by the investee as if it has sold a portion of its investment with any resulting gain or loss being reflected in earnings. EITF 08-6 is effective prospectively for interim periods and fiscal years beginning after December 15, 2008. We do not expect a material impact from the adoption of EITF 08-6.

## **RESULTS OF OPERATIONS**

Unless otherwise indicated, net sales in these results of operations are reported based upon the location where the sale was made. Certain prior year amounts have been reclassified to conform to the current year presentation. Please refer to Note 4 to the Consolidated Financial Statements for a reconciliation of segment operating income to consolidated earnings from continuing operations before income taxes.

In connection with its emergence from bankruptcy on October 2, 2006 (the "Effective Date"), AWI adopted fresh-start reporting in accordance with AICPA Statement of Position 90-7, "Financial Reporting by Entities in Reorganization under the Bankruptcy Code" ("SOP 90-7"). Adopting fresh-start reporting has resulted in material adjustments to the historical carrying amount of reorganized Armstrong's assets and liabilities. See Note 3 to the Consolidated Financial Statements for more information. As a result, our post-emergence financial statements are not comparable to our pre-emergence financial statements. Despite the lack of comparability, we have combined the 2006 results of the Predecessor Company (which represent the first nine months of 2006 and include the impact of emergence) with the results of the Successor Company (which represent the last three months of 2006) to facilitate the year-to-year discussion of operating results in certain sections of this Form 10-K. The combined financial information for 2006 is merely cumulative and does not give pro forma effect to the Predecessor's results as if the consummation of the Plan and the related fresh-start reporting and other adjustments had occurred at the beginning of the period presented. Combining pre-emergence and post-emergence results is not in accordance with GAAP.

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**2008 COMPARED TO 2007****CONSOLIDATED RESULTS**

	<u>Successor</u>		<u>Change is Favorable/ (Unfavorable)</u>	
	<u>Year 2008</u>	<u>Year 2007</u>	<u>As Reported</u>	<u>Excluding Effects of Foreign Exchange Rates <sup>(1)</sup></u>
<b>Net Sales:</b>				
Americas	\$ 2,384.4	\$ 2,614.7	(8.8)%	(9.1)%
Europe	826.0	774.4	6.7%	0.7%
Pacific Rim	<u>182.6</u>	<u>160.6</u>	13.7%	10.5%
<b>Total Consolidated Net Sales</b>	<b>\$ 3,393.0</b>	<b>\$ 3,549.7</b>	<b>(4.4)%</b>	<b>(6.0)%</b>
Cost of goods sold	2,632.0	2,687.5		
SG&A expense	579.9	611.3		
Intangible asset impairment	25.4	—		
Restructuring charges, net	0.8	0.2		
Equity earnings	<u>(56.0)</u>	<u>(46.0)</u>		
<b>Operating Income</b>	<b>\$ 210.9</b>	<b>\$ 296.7</b>		
Interest Expense	30.8	55.0		
Other non-operating expense	1.3	1.4		
Other non-operating (income)	(10.6)	(18.2)		
Chapter 11 reorganization (income), net	—	(0.7)		
Income tax expense	109.0	106.4		
(Gain) loss from discontinued operations	<u>(0.6)</u>	<u>7.5</u>		
<b>Net earnings</b>	<b><u>\$ 81.0</u></b>	<b><u>\$ 145.3</u></b>		

(1) Excludes favorable foreign exchange rate effect in translation of \$56.7 million on net sales and \$2.9 million on operating income.

Consolidated net sales, excluding the translation effect of changes in foreign exchange rates, declined 6%. Volume declines more than offset improvements in price realization (as described previously in "Pricing Initiatives") and an improved mix of higher value products.

Net sales in the Americas decreased approximately 9% as volume declines across the segments offset modest improvements in price realization and product mix in the Building Products and Resilient Flooring segments.

Excluding the translation effect of changes in foreign exchange rates, net sales in the European markets grew by \$6 million. Both Building Products and Resilient Flooring had modest price realization and improved product mix to offset lower volume.

Excluding the translation effect of changes in foreign exchange rates, net sales in the Pacific Rim increased \$18 million primarily due to volume growth.

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2008 and 2007 operating expenses were impacted by several significant items. The significant items which impacted cost of goods sold ("COGS"), selling, general and administrative expenses ("SG&A") and restructuring charges include:

Item	Where Reported	Successor	
		Year 2008	Year 2007
<b>Increase / (Reduction) in Expenses</b>			
<b>Fresh-Start : <sup>(1)</sup></b>			
Change in depreciation and amortization	COGS	\$ 7.9	\$ 2.1
Impact on hedging-related activity	COGS	—	(5.8)
Change in depreciation and amortization	SG&A	1.5	0.6
<b>Other Significant Items:</b>			
Cost reduction initiatives expenses <sup>(2)</sup>	COGS	7.3	—
Fixed asset impairment <sup>(3)</sup>	COGS	2.9	—
Cost reduction initiatives expenses <sup>(2)</sup>	SG&A	12.7	—
Insurance settlements <sup>(4)</sup>	SG&A	(6.9)	(5.0)
Environmental accrual <sup>(5)</sup>	SG&A	—	1.1
Chapter 11 related post-emergence (income) expenses <sup>(6)</sup>	SG&A	(1.3)	7.1
Review of strategic alternatives <sup>(7)</sup>	SG&A	1.2	8.7
Intangible asset impairment <sup>(8)</sup>	Intangible asset impairment	25.4	—
Cost reduction initiatives expenses <sup>(2)</sup>	Restructuring	0.8	0.2

- (1) See Note 3 for more information on fresh-start reporting.
- (2) See "Factors Affecting Operating Costs" and Notes 15 and 16 for a discussion of the cost reduction initiatives.
- (3) In 2008 we recorded a fixed asset impairment charge related to certain Resilient Flooring assets.
- (4) In 2008, we received an insurance settlement related to an environmental matter. In 2007, we received an insurance settlement related to a Cabinets warehouse fire.
- (5) We recorded an increase in the environmental accrual for a previously-owned property.
- (6) These costs represent professional and administrative fees incurred primarily to resolve remaining claims related to AWI's Chapter 11 Case and distribute proceeds to creditors, and expenses incurred by Armstrong Holdings, Inc., our former publicly held parent holding company, as it completed its plan of dissolution. In addition, 2008 includes the impact of the reversal of a contingent liability that was no longer owed to creditors after our final Chapter 11 distribution was made.
- (7) These expenses were incurred, primarily from advisors, in conducting our review of strategic alternatives.
- (8) During the fourth quarter of 2008, we recorded a non-cash impairment charge of \$25.4 million to reduce the carrying amount of our Wood Flooring trademarks to their estimated fair value based on the results of our annual impairment test.

Cost of goods sold in 2008 was 77.6% of net sales, compared to 75.7% in 2007. The year-to-year increase in the percentages is primarily due to lower sales to cover fixed costs. The change in the percentages was also impacted by the items detailed in the above table.

SG&A expenses in 2008 were \$579.9 million, or 17.1% of net sales compared to \$611.3 million or 17.2% of net sales in 2007. The year-to-year change was primarily due to the factors detailed in the above table offset by a significant decrease in unallocated corporate expense due to lower incentive compensation costs. In addition, most businesses reduced spending in response to lower sales volumes.

During the fourth quarter of 2008, we recorded a non-cash impairment charge of \$25.4 million to reduce the carrying amount of our Wood Flooring trademarks to their estimated fair value based on the results of our annual impairment test. The fair value was negatively affected by lower expected future cash flows due to the decline in the U.S. residential housing market. See Note 12 to the Consolidated Financial Statements for more information.



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Equity earnings, primarily from our WAVE joint venture, were \$56.0 million in 2008, as compared to \$46.0 million in 2007. See Note 11 for further information.

We recorded operating income of \$210.9 million in 2008, compared to operating income of \$296.7 million in 2007.

Interest expense was \$30.8 million in 2008, compared to \$55.0 million in 2007. The reduction was primarily due to lower debt balances and lower interest rates in 2008 compared to 2007.

Income tax expense from continuing operations was \$109.0 million and \$106.4 million in 2008 and 2007, respectively. The effective tax rate for 2008 was 57.6% as compared to a rate of 41.0% for 2007. The effective tax rate for 2008 was higher than 2007 due to additional valuation allowances on deferred state and foreign income tax assets and interest on uncertain tax positions. Partially offsetting these items was the tax benefit in 2008 for the costs incurred in 2007 for the review of strategic alternatives.

**REPORTABLE SEGMENT RESULTS**

**Resilient Flooring**

	<u>Successor</u>		<u>Change is Favorable/ (Unfavorable)</u>	
	<u>Year 2008</u>	<u>Year 2007</u>	<u>As Reported</u>	<u>Excluding Effects of Foreign Exchange Rates <sup>(1)</sup></u>
<b>Net Sales:</b>				
Americas	\$ 786.2	\$ 826.4	(4.9)%	(5.2)%
Europe	355.1	331.9	7.0%	(0.2)%
Pacific Rim	<u>78.8</u>	<u>72.5</u>	8.7%	5.9%
<b>Total Segment Net Sales</b>	<b>\$ 1,220.1</b>	<b>\$ 1,230.8</b>	<b>(0.9)%</b>	<b>(3.1)%</b>
<b>Operating (Loss) Income</b>	<b>\$ (16.8)</b>	<b>\$ 40.4</b>		

<sup>(1)</sup> Excludes favorable foreign exchange rate effect in translation of \$28.4 million on net sales and \$2.5 million on operating income.

Net sales in the Americas declined \$40.2 million. Volume declines due to broad weakness in residential markets and accelerating declines in commercial markets in the final two months of the year partially offset price realization and product mix improvement.

Excluding the translation effect of changes in foreign exchange rates, net sales in European markets were approximately flat as improved price and product mix offset lower volume.

Excluding the translation effect of changes in foreign exchange rates, net sales in the Pacific Rim grew \$4.4 million primarily due to improved product mix and modest price realization.

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Operating income decreased significantly due to lower volume in the Americas and global raw material inflation. In addition, both 2008 and 2007 operating profit were impacted by the previously described items as detailed in the following table.

Item	Increase / (Reduction) in Expenses	
	Year 2008	Year 2007
<b>Fresh-Start: <sup>(1)</sup></b>		
Change in depreciation and amortization	\$ 3.3	\$ 0.8
Impact on hedging-related activity		(1.5)
<b>Other Significant Items:</b>		
Cost reduction initiatives expenses <sup>(2)</sup>	14.1	—
Fixed asset impairment <sup>(3)</sup>	2.9	—
Environmental accrual <sup>(4)</sup>	—	1.1

(1) See Note 3 for more information on fresh-start reporting.

(2) See "Factors Affecting Operating Costs" and Note 15 for a discussion of the cost reduction initiatives.

(3) In 2008 we recorded a fixed asset impairment charge related to certain Resilient Flooring assets.

(4) We recorded an increase in the environmental accrual for a previously-owned property.

### Wood Flooring

Item	Successor		Change is (Unfavorable)
	Year 2008	Year 2007	
Total Segment Net Sales <sup>(1)</sup>	\$ 624.6	\$ 791.6	(21.1)%
Operating (Loss) Income	\$ (2.4)	\$ 64.3	

(1) Virtually all Wood Flooring products are sold in the Americas, primarily in the U.S.

Net sales decreased by \$167.0 million due to lower volume driven by continued declines in residential housing markets.

Operating income declined by \$66.7 million, primarily due to significantly lower sales. Reduced manufacturing and SG&A costs partially offset the decline in sales. In addition, 2008 operating profit was impacted by previously described items as detailed in the following table.

Item	Increase / (Reduction) in Expenses	
	Year 2008	Year 2007
<b>Fresh-Start: <sup>(1)</sup></b>		
Change in depreciation and amortization	\$ 1.0	\$ 0.2
<b>Other Significant Items:</b>		
Intangible asset impairment <sup>(2)</sup>	25.4	—

(1) See Note 3 for more information on fresh-start reporting.

(2) During the fourth quarter of 2008, we recorded a non-cash impairment charge of \$25.4 million to reduce the carrying amount of our Wood Flooring trademarks to their estimated fair value based on the results of our annual impairment test.

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**Building Products**

	Successor		Change is Favorable	
	Year 2008	Year 2007	As Reported	Excluding Effects of Foreign Exchange Rates <sup>(1)</sup>
<b>Net Sales:</b>				
Americas	\$ 794.4	\$ 761.5	4.3%	4.0%
Europe	470.9	442.5	6.4%	1.4%
Pacific Rim	103.8	88.1	17.8%	14.4%
<b>Total Segment Net Sales</b>	<b>\$ 1,369.1</b>	<b>\$ 1,292.1</b>	<b>6.0%</b>	<b>3.8%</b>
<b>Operating Income</b>	<b>\$ 239.7</b>	<b>\$ 221.4</b>	<b>8.3%</b>	<b>7.7%</b>

(1) Excludes favorable foreign exchange rate effect in translation of \$27.4 million on net sales and \$1.2 million on operating income.

The Americas net sales increased \$32.9 million. Price increases put in place to offset inflationary pressure and an improved product mix offset volume declines that accelerated in the fourth quarter. The improved product mix reflects a continued focus on developing and marketing high value products which satisfy today's design trends and higher acoustical performance needs.

Excluding the translation effect of changes in foreign exchange rates, net sales in Europe grew by \$6.4 million. The modest sales improvement was primarily due to improved price realization and volume growth in the emerging markets of Eastern Europe over the first three quarters of the year. These benefits offset growing volume declines in most Western European markets.

Excluding the translation effect of changes in foreign exchange rates, net sales in the Pacific Rim grew \$13.1 million on volume growth in Australia, China and India. The pace of growth in China and India significantly slowed in the fourth quarter of the year.

Operating income grew by \$18.3 million. Price realization, improved product mix and higher income from WAVE more than offset inflation in input costs and volume declines. In addition, 2008 and 2007 operating profit were impacted by previously described items as detailed in the following table.

Item	Increase / (Reduction) in Expenses	
	Year 2008	Year 2007
<b>Fresh-Start: <sup>(1)</sup></b>		
Change in depreciation and amortization	\$ 4.2	\$ 1.1
Impact on hedging-related activity	—	(4.3)
<b>Other Significant Items:</b>		
Cost reduction initiatives expenses <sup>(2)</sup>	—	0.2

(1) See Note 3 for more information on fresh-start reporting.

(2) These expenses relate to the closure of a Building Products plant in The Netherlands. Production ceased at this plant in 2005.

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**Cabinets**

	Successor		Change is (Unfavorable)
	Year 2008	Year 2007	
Total Segment Net Sales <sup>(1)</sup>	\$ 179.2	\$ 235.2	(23.8)%
Operating (Loss) Income	\$ (6.7)	\$ 10.5	

<sup>(1)</sup> All Cabinet products are sold in the U.S.

Net sales declined \$56.0 million on significant volume declines related to further deterioration in the U.S. housing markets.

Operating income was \$17.2 million worse than the prior year, primarily due to the decline in sales. In addition, 2007 operating profit was impacted by the previously described item as detailed in the following table.

**Increase / (Reduction) in Expenses**

Item	Successor	
	Year 2008	Year 2007
<b>Other Significant Items:</b>		
Insurance settlement <sup>(1)</sup>	—	\$ (5.0)

<sup>(1)</sup> We received an insurance settlement related to a warehouse fire.

**Unallocated Corporate**

Unallocated corporate expense of \$2.9 million in 2008 decreased from \$39.9 million in 2007. The decrease was primarily due to lower incentive compensation expense and reduced costs related to Chapter 11 and our review of strategic alternatives. In addition to costs related to Chapter 11 and our review of strategic alternatives, 2008 and 2007 operating profit were also impacted by previously described items as detailed in the following table.

**Increase / (Reduction) in Expenses**

Item	Successor	
	Year 2008	Year 2007
<b>Fresh-Start: <sup>(1)</sup></b>		
Change in depreciation and amortization	\$ 0.9	\$ 0.6
<b>Other Significant Items:</b>		
Cost reduction initiatives expenses <sup>(2)</sup>	6.7	—
Environmental insurance settlement <sup>(3)</sup>	(6.9)	—
Chapter 11 related post-emergence expenses <sup>(4)</sup>	(1.3)	7.1
Review of strategic alternatives <sup>(5)</sup>	1.2	8.7

<sup>(1)</sup> See Note 3 for more information on fresh-start reporting.

<sup>(2)</sup> Represents costs for corporate severances, partially offset by related reductions in stock compensation expense, and restructuring costs.

<sup>(3)</sup> We received an insurance settlement related to an environmental matter.

<sup>(4)</sup> These costs represent professional and administrative fees incurred primarily to resolve remaining claims related to AWI's Chapter 11 Case and distribute proceeds to creditors, and expenses incurred by Armstrong Holdings, Inc., our former publicly held parent holding company, as it completed its plan of dissolution. In addition, 2008 includes the impact of the reversal of a contingent liability that was no longer owed to creditors after our final Chapter 11 distribution was made.

<sup>(5)</sup> These expenses were incurred, primarily from advisors, in conducting our review of strategic alternatives.



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**FINANCIAL CONDITION AND LIQUIDITY**Cash Flow

The Consolidated Statements of Cash Flows combine the cash flows generated from discontinued operations with the cash flows from continuing operations within operating, investing and financing activities. Cash flows from discontinued operations were not material for each cash flow category. The absence of these cash flows from discontinued operations will not materially affect our future liquidity and capital resources.

As shown on the Consolidated Statements of Cash Flows, our cash and cash equivalents balance decreased by \$159.3 million in 2008 compared to an increase of \$250.5 million in 2007.

Operating activities in 2008 provided \$214.2 million of net cash, primarily due to cash earnings and distributions from WAVE of \$61.0 million (which includes a special distribution of \$5.5 million). These were partially offset by a reduction in accounts payable and accrued expenses of \$88.2 million, primarily due to lower activity and the payment of incentive accruals during the first quarter of 2008. Operating activities in 2007 provided \$575.2 million of net cash, primarily due to cash earnings, net U.S. federal income tax refunds of \$209.1 million and distributions from WAVE of \$117.5 million (which includes special distributions of \$50.0 million).

Investing activities in 2008 used \$75.7 million of cash primarily due to capital expenditures of \$95.0 million, partially offset by a special distribution from WAVE of \$19.5 million, which was classified as a return of investment. Investing activities in 2007 used \$36.7 million of cash primarily due to capital expenditures of \$102.6 million partially offset by proceeds received from the divestiture of a business of \$58.8 million.

Financing activities in 2008 used \$277.0 million primarily due to a special cash dividend of \$256.4 million. Financing activities used \$305.4 million of cash in 2007 primarily due to voluntary principal debt prepayments of \$300 million.

Balance Sheet and Liquidity

Changes in significant balance sheet accounts and groups of accounts from December 31, 2007 to December 31, 2008 are as follows:

	<u>Successor Company</u>		<u>Decrease</u>
	<u>December 31,</u> <u>2008</u>	<u>December 31,</u> <u>2007</u>	
Cash and cash equivalents	\$ 355.0	\$ 514.3	\$ (159.3)
Current assets, excluding cash and cash equivalents	906.5	976.2	(69.7)
Current assets	<u>\$ 1,261.5</u>	<u>\$ 1,490.5</u>	<u>\$ (229.0)</u>

The decrease in cash and cash equivalents was described above (see "Cash Flow"). The decrease in current assets, excluding cash and cash equivalents, is primarily due to lower levels of accounts receivable due to lower sales in November and December of 2008 compared to the comparative periods of 2007.

	<u>December 31,</u> <u>2008</u>	<u>December 31,</u> <u>2007</u>	<u>Decrease</u>
Property, plant and equipment, less accumulated depreciation and amortization ("PP&E")	\$ 954.2	\$ 1,012.8	\$ (58.6)

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The decrease in PP&E was primarily due to depreciation of \$135.5 million and the effects of foreign exchange of approximately \$20 million. These were partially offset by capital expenditures of \$95.0 million.

	December 31, 2008	December 31, 2007	Decrease
Prepaid pension costs	\$ 0.3	\$ 708.0	\$ (707.7)

The decrease in prepaid pension costs occurred primarily because four of our previously overfunded pension plans became underfunded in relation to their benefit obligations as of December 31, 2008 primarily due to the impact of lower asset values in 2008. Therefore, the net underfunded position of these pension plans is recorded within Pension Benefit Liabilities.

	December 31, 2008	December 31, 2007	Decrease
Investment in affiliates	\$ 208.2	\$ 232.6	\$ (24.4)

The decrease in investments in affiliates was primarily due to distributions from WAVE of \$80.5 million (including a special distribution of \$25 million) partially offset by equity earnings of \$56.0 million.

	December 31, 2008	December 31, 2007	Increase (Decrease)
Deferred income tax assets, current	\$ 14.4	\$ 43.5	\$ (29.1)
Deferred income tax assets, noncurrent	219.6	424.5	(204.9)
Deferred income tax liabilities, current	(4.6)	(29.5)	24.9
Deferred income tax liabilities, noncurrent	(9.0)	(471.4)	462.4
	<u>\$ 220.4</u>	<u>\$ (32.9)</u>	<u>\$ 253.3</u>

See Note 17 for further information on income taxes.

	December 31, 2008	December 31, 2007	Increase (Decrease)
Current installments of long-term debt	\$ 40.9	\$ 24.7	\$ 16.2
Long-term debt, less current installments	454.8	485.8	(31.0)
Long-term debt	<u>\$ 495.7</u>	<u>\$ 510.5</u>	<u>\$ (14.8)</u>

The decrease in long-term debt was primarily due to scheduled debt repayments of \$20.9 million.

#### Liquidity

Our liquidity needs for operations vary throughout the year. We retain lines of credit to facilitate our seasonal needs. On October 2, 2006, Armstrong executed a \$1.1 billion senior credit facility with Bank of America, N.A., JPMorgan Chase Bank, N.A. and Barclays Bank PLC. This facility was made up of a \$300 million revolving credit facility (with a \$150 million sublimit for letters of credit), a \$300 million Term Loan A (due in 2011), and a \$500 million Term Loan B (due in 2013). There were no outstanding borrowings under the revolving credit facility, but \$49.6 million in letters of credit were outstanding as of December 31, 2008 and, as a result, availability under the revolving credit facility was \$250.4 million.

On December 31, 2008 we also had outstanding letters of credit totaling \$10.4 million arranged with another bank. Letters of credit are issued to third party suppliers, insurance and financial institutions and typically can only be drawn upon in the event of AWI's failure to pay its obligations to the beneficiary.

As of December 31, 2008, we have \$355.0 million of cash and cash equivalents, \$202.5 million in the U.S. and \$152.5 million in various foreign jurisdictions.

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On February 25, 2008, we executed an amendment to our senior credit facility. This amendment (a) permits us to make "Special Distributions," including dividends (such as the special cash dividend described below) or other distributions (whether in cash, securities or other property) of up to an aggregate of \$500 million at any time prior to February 28, 2009, (b) requires that we maintain minimum domestic liquidity of at least \$100 million as of March 31, June 30, September 30 and December 31 of each year, which may be comprised of a combination of cash and cash equivalents and undrawn commitments under our revolving credit facility and (c) increases by 0.25% the borrowing margins in the pricing grid set forth in the facility for the revolving credit facility and Term Loan A. We do not anticipate extending the amendment beyond February 28, 2009. As of December 31, 2008 our domestic liquidity was \$452.9 million.

In addition to the minimum domestic liquidity covenant, our credit facility contains two other financial covenants: minimum Interest Coverage (minimum 3.00 to 1.00) and maximum Indebtedness to EBITDA (Earnings Before Interest Taxes and Depreciation) (maximum 3.75 to 1.00), as defined in the credit facility (incorporated in this 10-K as Exhibit 10.10). As of December 31, 2008 our consolidated interest coverage ratio was 12.98 to 1.00 and our indebtedness to EBITDA was 1.24 to 1.00. Management believes that based on current financial projections the likelihood of default under these covenants is unlikely. Fully borrowing under our revolving credit facility, provided we maintain minimum domestic liquidity of \$100 million, would not violate these covenants.

Prepayments of the loans under the senior credit facility are required unless (a) the Consolidated leverage ratio is less than or equal to 2.5:1.0, and (b) debt ratings from S&P is BB (stable) or better and from Moody's is Ba2 (stable) or better. If required, the prepayment amount would be 50% of Consolidated Excess Cash Flow (as defined in the credit facility, incorporated in this 10-K as Exhibit 10.10). Mandatory prepayments have not occurred since the inception of the agreement. Our current debt rating from S&P is BB (stable) and from Moody's is Ba2 (stable).

On February 25, 2008, our Board of Directors declared a special cash dividend of \$4.50 per common share, payable on March 31, 2008, to shareholders of record on March 11, 2008. This special cash dividend resulted in an aggregate payment to our shareholders of \$256.4 million. The Board will continue to evaluate the return of cash to shareholders based on factors including actual and forecasted operating results, the outlook for global economies and credit markets, and the Company's current and forecasted capital requirements.

As of December 31, 2008, our foreign subsidiaries had available lines of credit totaling \$32.3 million, of which \$2.8 million was used and \$4.9 million was available only for letters of credit and guarantees, leaving \$24.6 million of unused lines of credit available for foreign borrowings. However, these lines of credit are uncommitted, and poor operating results or credit concerns at the related foreign subsidiaries could result in the lines being withdrawn by the lenders. We have been able to maintain and, as needed, replace credit facilities to support our foreign operations.

In October 2007 we received \$178.7 million of federal income tax refunds (see Note 17). Upon receipt of the refunds, AWI recorded a liability of \$144.6 million in the fourth quarter of 2007. The tax refunds are subject to examination and adjustment by the Internal Revenue Service ("IRS") under its normal audit procedure. We are currently under examination for the 2005 and 2006 tax years.

We believe that cash on hand and generated from operations, together with lines of credit and the availability under the \$300 million revolving credit facility, will be adequate to address our foreseeable liquidity needs based on current expectations of our business operations and for scheduled payments of debt obligations.

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**2007 COMPARED TO 2006****CONSOLIDATED RESULTS**

	Successor	Successor	Predecessor	Combined	Change is Favorable/ (Unfavorable)	
	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006	Year 2006	Reported	Excluding Effects of Foreign Exchange Rates <sup>(1)</sup>
<b>Net Sales:</b>						
Americas	\$ 2,614.7	\$ 606.9	\$ 2,011.3	\$ 2,618.2	(0.1)%	(0.4)%
Europe	774.4	172.2	499.4	671.6	15.3%	6.0%
Pacific Rim	160.6	38.2	97.9	136.1	18.0%	10.6%
<b>Total Consolidated Net Sales</b>	<b>\$ 3,549.7</b>	<b>\$ 817.3</b>	<b>\$ 2,608.6</b>	<b>\$ 3,425.9</b>	<b>3.6%</b>	<b>1.3%</b>
Cost of goods sold	2,687.5	660.9	2,030.2	2,691.1		
SG&A expense	611.3	143.5	415.5	559.0		
Restructuring charges, net	0.2	1.7	10.0	11.7		
Equity earnings	(46.0)	(5.3)	(41.4)	(46.7)		
<b>Operating Income</b>	<b>\$ 296.7</b>	<b>\$ 16.5</b>	<b>\$ 194.3</b>	<b>\$ 210.8</b>		
Interest Expense	55.0	13.4	5.2	18.6		
Other non-operating expense	1.4	0.3	1.0	1.3		
Other non-operating (income)	(18.2)	(4.3)	(7.2)	(11.5)		
Chapter 11 reorganization (income), net	(0.7)	—	(1,955.5)	(1,955.5)		
Income tax expense	106.4	3.8	726.6	730.4		
Loss from discontinued operations	7.5	1.1	68.4	69.5		
<b>Net earnings</b>	<b>\$ 145.3</b>	<b>\$ 2.2</b>	<b>\$ 1,355.8</b>	<b>\$ 1,358.0</b>		

<sup>(1)</sup> Excludes favorable foreign exchange rate effect in translation of \$78.4 million on net sales and \$2.1 million on operating income.

Consolidated net sales excluding the translation effect of changes in foreign exchange rates grew 1%. Equal benefits from price realization (approximately \$60 million, as described previously in "Pricing Initiatives") and an improved mix of higher value products more than offset low single-digit volume decline.

Net sales in the Americas was essentially flat. Volume declined in the Wood Flooring and Resilient Flooring businesses. Net sales of Building Products and Resilient Flooring products benefited from a richer product mix, and Building Products realized price increases.

Excluding the translation effect of changes in foreign exchange rates, net sales in the European markets grew by \$42 million due to a combination of volume growth, price realization and higher-value product mix.

Excluding the translation effect of changes in foreign exchange rates, net sales in the Pacific Rim increased \$15 million on volume growth and improved product mix.

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Operating expenses in the year 2007 and the three months ended December 31, 2006 were impacted by the effects of having adopted fresh-start reporting, as a result of AWI emerging from Chapter 11. Adopting fresh-start reporting resulted in material adjustments to the historical carrying amount of reorganized Armstrong's assets and liabilities. Certain of these adjustments impacted our statements of earnings for the periods following emergence, through changes in the items noted in the chart below. The amounts represent the post-emergence change in these items. Net sales were not impacted by fresh-start reporting. In addition, 2007 and 2006 operating expenses were impacted by several other significant items. The fresh-start and other significant items, which impacted cost of goods sold ("COGS"), selling, general and administrative expenses ("SG&A"), restructuring charges and equity earnings, include:

**Increase / (Reduction) in Expenses**

Item	Where Reported	Successor	Successor	Predecessor
		Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
<b>Fresh-Start:</b> <sup>(1)</sup>				
Change in depreciation and amortization	COGS	\$ (2.1)	\$ (1.3)	—
Change in costs for benefit plans	COGS	(20.2)	(4.6)	—
Impact on hedging-related activity	COGS	(5.8)	(1.0)	—
Inventory-related costs	COGS	—	29.6	—
Change in depreciation and amortization	SG&A	11.6	2.8	—
Change in costs for benefit plans	SG&A	(11.3)	(2.3)	—
Inventory-related costs (WAVE)	Equity Earnings	—	3.7	—
Expenses from WAVE step-up	Equity Earnings	6.7	1.7	—
<b>Other Significant Items:</b>				
Business interruption claim <sup>(2)</sup>	COGS	—	(4.7)	—
Cost reduction initiatives expenses <sup>(3)</sup>	COGS	—	0.7	\$ 10.3
Product warranty accrual <sup>(4)</sup>	COGS	—	—	3.3
Contribution to Armstrong Foundation <sup>(5)</sup>	SG&A	—	—	5.0
Liability settlement related to a divested business <sup>(6)</sup>	SG&A	—	—	2.8
Patent infringement settlement <sup>(7)</sup>	SG&A	—	—	(8.6)
Cost reduction initiatives expenses <sup>(3)</sup>	SG&A	—	—	7.4
Gain on sale of properties <sup>(8)</sup>	SG&A	—	—	(17.0)
Insurance settlement <sup>(9)</sup>	SG&A	(5.0)	—	—
Environmental accrual <sup>(10)</sup>	SG&A	1.1	—	—
Chapter 11 related post-emergence expenses <sup>(11)</sup>	SG&A	7.1	4.6	—
Review of strategic alternatives <sup>(12)</sup>	SG&A	8.7	—	—
Cost reduction initiatives expenses <sup>(3)</sup>	Restructuring	0.2	1.6	10.1

(1) See Note 3 for more information on fresh-start reporting.

(2) In the fourth quarter of 2006, we received the final payment for a business interruption claim.

(3) See "Factors Affecting Operating Costs" and Note 16 for a discussion on the cost reduction expenses.

(4) The majority of the product warranty accrual increase was from revising certain assumptions that were used in prior periods when estimating the accrual.

(5) We made a contribution to the Armstrong Foundation (a community giving program funded by Armstrong) in the third quarter of 2006.

(6) We settled a liability related to a previously divested business in the third quarter of 2006 for an amount greater than what was previously accrued.

(7) In the first quarter of 2006, we recorded a gain from the settlement of a patent infringement case.

(8) During the year 2006, we recorded a gain from the sale of two buildings.

(9) We received an insurance settlement related to a Cabinets warehouse fire.

(10) We recorded an increase in the environmental accrual for a previously-owned property.



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- (11) These costs represent professional and administrative fees incurred primarily to resolve remaining claims related to AWI's Chapter 11 Case and distribute proceeds to creditors, and expenses incurred by Armstrong Holdings, Inc. as it completed its plan of dissolution.
- (12) These expenses were incurred, primarily from advisors, in conducting our review of strategic alternatives.

Cost of goods sold in 2007 was 75.7% of net sales, compared to 78.6% in 2006. The year-to-year change in the percentages is primarily due to the items detailed in the above table. In addition, 2007 benefited from higher selling prices, primarily in Building Products, and better manufacturing performance across most segments, which more than offset raw material inflation in Building Products and Wood Flooring.

SG&A expenses in 2007 were \$611.3 million, or 17.2% of net sales compared to \$559.0 million or 16.3% of net sales in 2006. The year-to-year change in the percentages was primarily due to the factors detailed in the above table. In addition, unallocated corporate expense increased due to higher benefit plan costs. Building Products increased spending to support its sales growth, but at a rate below the growth in sales.

Equity earnings, primarily from our WAVE joint venture, were \$46.0 million in 2007, as compared to \$46.7 million in 2006. Equity earnings in 2007 and 2006 were impacted by the items as detailed in the above table. See Note 11 for further information.

We recorded operating income of \$296.7 million in 2007, compared to operating income of \$210.8 million in 2006.

Interest expense was \$55.0 million in 2007, compared to \$18.6 million in 2006. Interest expense in both years was impacted by debt incurred as part of emerging from Chapter 11, although for only three months in 2006. In accordance with SOP 90-7, we did not record contractual interest expense on prepetition debt while in Chapter 11. This unrecorded interest expense was \$57.6 million in 2006. Unrecorded interest expense reflects the amount of interest expense we would have incurred under the original maturities of prepetition debt.

Net Chapter 11 reorganization income in 2007 was \$0.7 million compared to \$1,955.5 million recorded in 2006. See Note 1 to the Consolidated Financial Statements for a detailed breakout of the 2007 and 2006 amounts.

Income tax expense was \$106.4 million and \$730.4 million in 2007 and 2006, respectively. The effective tax rate for 2007 was 41.0% as compared to a rate of 33.8% for 2006. Excluding the effect of fresh-start reporting and POR-related settlement adjustments, the 2006 effective tax rate was 38.3%. The effective tax rate for 2007 was higher than 2006 due to increased state income taxes, taxes on foreign source income and a reduced Medicare subsidy, partially offset by a reduction in nondeductible professional fees related to our Chapter 11 emergence and the review of strategic alternatives.

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**REPORTABLE SEGMENT RESULTS****Resilient Flooring**

	Successor Year 2007	Successor Three Months Ended December 31, 2006	Predecessor Nine Months Ended September 30, 2006	Combined Year 2006	Change is Favorable/ (Unfavorable)	
					As Reported	Excluding Effects of Foreign Exchange Rates <sup>(1)</sup>
<b>Net Sales:</b>						
Americas	\$ 826.4	\$ 187.0	\$ 662.6	\$ 849.6	(2.7)%	(3.1)%
Europe	331.9	74.2	223.2	297.4	11.6%	2.0%
Pacific Rim	72.5	17.3	43.6	60.9	19.0%	11.5%
<b>Total Segment Net Sales</b>	<b>\$ 1,230.8</b>	<b>\$ 278.5</b>	<b>\$ 929.4</b>	<b>\$ 1,207.9</b>	<b>1.9%</b>	<b>(1.1)%</b>
<b>Operating Income (Loss)</b>	<b>\$ 40.4</b>	<b>\$ (1.2)</b>	<b>\$ 12.6</b>	<b>\$ 11.4</b>		

(1) Excludes favorable foreign exchange rate effect in translation of \$35.9 million on net sales and \$1.5 million on operating income.

Net sales in the Americas declined \$23.2 million. Volume declined at a mid-single digit rate due to weakness in residential products, pricing was flat and product mix improved on growth in the sales of higher-value laminate and vinyl sheet products.

Excluding the translation effect of changes in foreign exchange rates, net sales in the European markets grew \$6.4 million, primarily due to increased volume.

Excluding the translation effect of changes in foreign exchange rates, net sales in the Pacific Rim grew \$7.2 million, primarily due to volume growth.

Operating income improved significantly, despite soft sales, due to lower manufacturing costs and reduced SG&A expenses. In addition, both 2007 and 2006 operating profit were impacted by the previously described items as detailed in the following table.

**Increase / (Reduction) in Expenses**

Item	Successor	Successor	Predecessor
	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
<b>Fresh-Start: <sup>(1)</sup></b>			
Change in depreciation and amortization	\$ (1.0)	\$ (0.8)	—
Change in costs for benefit plans	(5.5)	(0.8)	—
Impact on hedging-related activity	(1.5)	(0.2)	—
Inventory-related costs	—	7.2	—
<b>Other Significant Items:</b>			
Business interruption claim <sup>(2)</sup>	—	(4.7)	—
Cost reduction initiative expenses <sup>(3)</sup>	—	0.8	\$ 26.6
Gain on sale of properties <sup>(4)</sup>	—	—	(17.0)
Environmental accrual <sup>(5)</sup>	1.1	—	—

(1) See Note 3 for more information on fresh-start reporting.

(2) In the fourth quarter of 2006, we received the final payment for a business interruption claim.

(3) See "Factors Affecting Operating Costs" for a discussion on the cost reduction expenses.

(4) During 2006, we recorded a gain from the sale of two buildings.



(5) We recorded an increase in the environmental accrual for a previously-owned property.

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**Wood Flooring**

	<u>Successor</u>	<u>Successor</u> Three Months Ended December 31, 2006	<u>Predecessor</u> Nine Months Ended September 30, 2006	<u>Combined</u> Year 2006	Change is (Unfavorable)
Total Segment Net Sales <sup>(1)</sup>	\$ 791.6	\$ 192.6	\$ 645.0	\$ 837.6	(5.5)%
Operating Income	\$ 64.3	\$ (0.2)	\$ 46.2	\$ 46.0	

<sup>(1)</sup> Virtually all Wood Flooring products are sold in the Americas, primarily in the U.S.

Net sales decreased by \$46.0 million due to lower volume driven by declines in the residential housing market.

Operating income increased by \$18.3 million due to the previously described items as detailed in the following table. In addition, declining sales volume and raw material inflation more than offset improved manufacturing productivity. 2007 operating income included a \$2.7 million SG&A expense for an increase to the reserve for doubtful accounts receivable related to a distributor.

**Increase / (Reduction) in Expenses**

<u>Item</u>	<u>Successor</u> Year 2007	<u>Successor</u> Three Months Ended December 31, 2006	<u>Predecessor</u> Nine Months Ended September 30, 2006
<b>Fresh-Start: <sup>(1)</sup></b>			
Change in depreciation and amortization	\$ (13.3)	\$ (3.4)	—
Inventory-related costs	—	12.4	—
<b>Other Significant Items:</b>			
Cost reduction initiatives expenses <sup>(2)</sup>	—	1.4	\$ 0.7
Product warranty accrual <sup>(3)</sup>	—	—	3.3

(1) See Note 3 for more information on fresh-start reporting.

(2) These expenses related primarily to the shutdown of manufacturing plants in Nashville, Tennessee and Searcy, Arkansas.

(3) The majority of the product warranty accrual increase was from revising certain assumptions that were used in prior periods when estimating the accrual.

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**Building Products**

	<u>Successor</u>	<u>Successor</u>	<u>Predecessor</u>	<u>Combined</u>	<u>Change is Favorable</u>	
	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006	Year 2006	As Reported	Excluding Effects of Foreign Exchange Rates <sup>(1)</sup>
<b>Net Sales:</b>						
Americas	\$ 761.5	\$ 170.8	\$ 529.3	\$ 700.1	8.8%	8.3%
Europe	442.5	98.0	276.2	374.2	18.3%	9.1%
Pacific Rim	88.1	20.9	54.3	75.2	17.2%	9.8%
<b>Total Segment Net Sales</b>	<b>\$ 1,292.1</b>	<b>\$ 289.7</b>	<b>\$ 859.8</b>	<b>\$ 1,149.5</b>	<b>12.4%</b>	<b>8.7%</b>
Operating Income	\$ 221.4	\$ 24.9	\$ 152.9	\$ 177.8		

(1) Excludes favorable foreign exchange rate effect in translation of \$40.7 million on net sales and \$3.5 million on operating income.

The Americas net sales increased \$61.4 million. The improvement was primarily driven by price increases across the majority of channels and a more favorable mix of products. The improved product mix reflects a continued focus on developing and marketing high value products which satisfy today's design trends and higher acoustical performance needs.

Excluding the translation effect of changes in foreign exchange rates, net sales in Europe grew by \$35.9 million. The sales improvement was driven equally by volume growth and improved pricing across both Western and Eastern Europe.

Excluding the translation effect of changes in foreign exchange rates, net sales in the Pacific Rim grew \$7.5 million on strong sales in India, Australia and China.

Operating income increased by \$43.6 million due to sales growth and improved manufacturing productivity. These benefits were partially offset by inflation in direct production costs and by increased investment in SG&A to support the sales growth. In addition, both 2007 and 2006 operating profit were impacted by the previously described items as detailed in the following table.

**Increase / (Reduction) in Expenses**

<b>Item</b>	<u>Successor</u>	<u>Successor</u>	<u>Predecessor</u>
	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
<b>Fresh-Start: <sup>(1)</sup></b>			
Change in depreciation and amortization	\$ 22.1	\$ 5.2	—
Change in costs for benefit plans	(6.3)	(1.3)	—
Impact on hedging-related activity	(4.3)	(0.8)	—
Inventory-related costs	—	9.2	—
Inventory-related costs (WAVE)	—	3.7	—
Expenses from WAVE step-up	6.7	1.7	—
<b>Other Significant Items:</b>			
Cost reduction initiatives expenses <sup>(2)</sup>	0.2	0.1	\$ 0.6

(1) See Note 3 for more information on fresh-start reporting.

(2) These expenses related to the closure of a plant in The Netherlands.



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**Cabinets**

	<u>Successor</u>	<u>Successor</u> Three Months Ended December 31, 2006	<u>Predecessor</u> Nine Months Ended September 30, 2006	<u>Combined</u> Year 2006	Change is Favorable
Total Segment Net Sales <sup>(1)</sup>	\$ 235.2	\$ 56.5	\$ 174.4	\$ 230.9	1.9%
Operating Income	\$ 10.5	\$ 0.2	\$ 6.1	\$ 6.3	

(1) All Cabinet products are sold in the U.S.

Net sales grew \$4.3 million as growth in the first half of the year was largely offset by declines in the second half related to deterioration in the U.S. housing market.

Operating income grew \$4.2 million due to the previously described items as detailed in the following table. In addition, operating income was reduced by manufacturing inefficiencies.

**Increase / (Reduction) in Expenses**

<u>Item</u>	<u>Successor</u> Year 2007	<u>Successor</u> Three Months Ended December 31, 2006	<u>Predecessor</u> Nine Months Ended September 30, 2006
<b>Fresh-Start:</b> <sup>(1)</sup>			
Change in depreciation and amortization	\$ (0.3)	\$ 0.1	—
Inventory-related costs	—	0.8	—
<b>Other Significant Items:</b>			
Insurance settlement <sup>(2)</sup>	(5.0)	—	—

(1) See Note 3 for more information on fresh-start reporting.

(2) We received an insurance settlement related to a warehouse fire.

Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

**Unallocated Corporate**

Unallocated corporate expense of \$39.9 million in 2007 increased from \$30.7 million in 2006 (\$7.2 million in the three months ended December 31, 2006 and \$23.5 million in the nine months ended September 30, 2006). The changes were primarily due to higher benefit plan costs and the previously described items as detailed in the following table.

Item	<b>Increase / (Reduction) in Expenses</b>		
	<u>Successor</u> Year 2007	<u>Successor</u> Three Months Ended December 31, 2006	<u>Predecessor</u> Nine Months Ended September 30, 2006
<b>Fresh-Start:</b> <sup>(1)</sup>			
Change in depreciation and amortization	\$ 2.0	\$ 0.3	—
Change in costs for benefit plans	(19.7)	(4.8)	—
<b>Other Significant Items:</b>			
Cost reduction initiatives expenses <sup>(2)</sup>	—	—	\$ (0.1)
Contribution to Armstrong Foundation <sup>(3)</sup>	—	—	5.0
Liability settlement related to a divested business <sup>(4)</sup>	—	—	2.8
Patent infringement settlement <sup>(5)</sup>	—	—	(8.6)
Chapter 11 related post-emergence expenses <sup>(6)</sup>	7.1	4.6	
Review of strategic alternatives <sup>(7)</sup>	8.7	—	—

(1) See Note 3 for more information on fresh-start reporting.

(2) These costs related primarily to cost reduction actions that were initiated in prior years.

(3) We made a contribution to the Armstrong Foundation (a community giving program funded by Armstrong) in the third quarter of 2006.

(4) We settled a liability related to a previously divested business in the third quarter of 2006 for an amount greater than what was previously accrued.

(5) In the first quarter of 2006, we recorded a gain from the settlement of a patent infringement case.

(6) These costs represent professional and administrative fees incurred primarily to resolve remaining claims related to AWI's Chapter 11 Case and distribute proceeds to creditors, and expenses incurred by Armstrong Holdings, Inc. as it completed its plan of dissolution.

(7) These expenses were incurred, primarily from advisors, in conducting our review of strategic alternatives.

**FINANCIAL CONDITION AND LIQUIDITY**Cash Flow

The Consolidated Statements of Cash Flows combine the cash flows generated from discontinued operations with the cash flows from continuing operations within operating, investing and financing activities. Cash flows from discontinued operations were not material for each cash flow category. The absence of these cash flows from discontinued operations will not materially affect our future liquidity and capital resources.

As shown on the Consolidated Statements of Cash Flows, our cash and cash equivalents balance increased by \$250.5 million in 2007 compared to a decrease of \$338.4 million in 2006.

Operating activities in 2007 provided \$575.2 million of net cash, primarily due to cash earnings, net U.S. federal income tax refunds of \$209.1 million and distributions from WAVE of \$117.5 million. In 2006 operating activities used \$633.0 million (\$95.1 million provided in the three months ended December 31, 2006 and \$728.1 million used in the nine months ended September 30, 2006) primarily due to the settlement of liabilities subject to compromise (excluding prepetition debt) of \$832.7 million.

Investing activities in 2007 used \$36.7 million of cash primarily due to capital expenditures of \$102.6 million partially offset by proceeds received from the divestiture of a business of \$58.8 million. In 2006 investing activities used \$172.0 million (\$40.3 million used in the three months ended December 31, 2006 and \$131.7 million used in the nine months ended September 30, 2006) due to capital expenditures of



Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

\$138.5 million and cash paid for acquisitions of \$60.5 million, which were partially offset by proceeds from the sale of assets of \$39.1 million. Year-to-year, capital expenditures decreased approximately \$36 million as all our businesses were able to reduce their investments, partially due to prior years' spending, while still maintaining our operations.

Financing activities used \$305.4 million of cash in 2007 primarily due to voluntary principal debt prepayments of \$300 million. In 2006 financing activities provided \$459.9 million (\$8.1 million used in the three months ended December 31, 2006 and \$468.0 million provided in the nine months ended September 30, 2006) due to the receipt of \$800 million from the issuance of new debt upon emergence partially offset by payments of \$300.7 million made as part of discharging the debt-related portion of liabilities subject to compromise.

### **OFF-BALANCE SHEET ARRANGEMENTS**

No disclosures are required pursuant to Item 303(a)(4) of Regulation S-K.

### **CONTRACTUAL OBLIGATIONS**

As part of our normal operations, we enter into numerous contractual obligations that require specific payments during the term of the various agreements. The following table includes amounts ongoing under contractual obligations existing as of December 31, 2008. Only known payments that are dependent solely on the passage of time are included. Obligations under contracts that contain minimum payment amounts are shown at the minimum payment amount. Contracts that have variable payment structures without minimum payments are excluded. Purchase orders that are entered into in the normal course of business are also excluded because they are generally cancelable and not legally binding. Amounts are presented below based upon the currently scheduled payment terms. Actual future payments may differ from the amounts presented below due to changes in payment terms or events leading to payments in addition to the minimum contractual amounts.

	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>Thereafter</u>	<u>Total</u>
Long-Term Debt	\$ 40.9	\$ 32.3	\$ 234.8	\$ 3.5	\$ 184.1	\$ 0.1	\$ 495.7
Scheduled Interest Payments <sup>(1)</sup>	15.0	16.1	16.8	10.2	8.1	—	66.2
Capital Lease Obligations <sup>(2)</sup>	—	—	—	—	—	0.1	0.1
Operating Lease Obligations <sup>(2)</sup>	14.9	10.6	6.7	3.5	2.1	4.7	42.5
Unconditional Purchase Obligations <sup>(3)</sup>	13.8	12.6	1.7	0.4	—	—	28.5
Other Long-Term Obligations <sup>(4), (5)</sup>	9.3	0.4	0.1	—	—	—	9.8
<b>Total Contractual Obligations</b>	<b><u>\$ 93.9</u></b>	<b><u>\$ 72.0</u></b>	<b><u>\$ 260.1</u></b>	<b><u>\$ 17.6</u></b>	<b><u>\$ 194.3</u></b>	<b><u>\$ 4.9</u></b>	<b><u>\$ 642.8</u></b>

(1) For debt with variable interest rates, we projected future interest payments based on January 31, 2009 interest rates.

(2) Capital and operating lease obligations include the minimum lease payments due under existing lease agreements with noncancelable lease terms in excess of one year.

(3) Unconditional purchase obligations include (a) purchase contracts whereby we must make guaranteed minimum payments of a specified amount regardless of how little material is actually purchased ("take or pay" contracts) and (b) service agreements. Unconditional purchase obligations exclude contracts entered into during the normal course of business that are non-cancelable and have fixed per unit fees, but where the monthly commitment varies based upon usage. Cellular phone contracts are an example.

(4) Other long-term obligations include payments under severance agreements.

(5) Other long-term obligations does not include \$174.4 million of liabilities under FIN 48. Of this amount, \$146.4 million relates to the utilization of a 10-year carryback of net operating losses created by funding the Asbestos PI Trust under AWI's POR in October 2006. Due to the uncertainty relating to this and other positions, we are unable to reasonably estimate the ultimate amount or timing of the settlement of these issues. See Note 17 to the Consolidated Financial Statements for more information.



Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

We have issued financial guarantees to assure payment on behalf of our subsidiaries in the event of default on various debt and lease obligations in the table above. We have not issued any guarantees on behalf of joint-venture or unrelated businesses.

We are party to supply agreements, some of which require the purchase of inventory remaining at the supplier upon termination of the agreement. The last such agreement will expire in 2010. Had these agreements terminated at December 31, 2008, Armstrong would have been obligated to purchase approximately \$17.5 million of inventory. Historically, due to production planning, we have not had to purchase material amounts of product at the end of similar contracts. Accordingly, no liability has been recorded for these guarantees.

As part of our executive compensation plan, certain current and former executives participate in a split-dollar insurance program where we are responsible for remitting the premiums. Since 1998, the program was closed to new participants. As of December 31, 2008, we carried a cash surrender value asset of \$9.0 million related to this program. Should we discontinue making premium payments, the insured executives have the right to the entire policy cash surrender value. In light of the Sarbanes-Oxley Act, we believe it is inappropriate to make the premium payments for three of the executives participating in this plan. As a result, we have required these three individuals to make the premium payments to continue the policy.

We utilize lines of credit and other commercial commitments in order to ensure that adequate funds are available to meet operating requirements. Letters of credit are issued to third party suppliers, insurance and financial institutions and typically can only be drawn upon in the event of our failure to pay our obligations to the beneficiary. This table summarizes the commitments we have available for use as of December 31, 2008. Letters of credit are currently arranged through our revolving credit facility. Certain letters of credit arranged with another bank prior to our Chapter 11 filing remain outstanding.

<u>Other Commercial Commitments</u>	<u>Total Amounts Committed</u>	<u>Less Than 1 Year</u>	<u>1 – 3 Years</u>	<u>4 – 5 Years</u>	<u>Over 5 Years</u>
Letters of Credit	\$ 60.0	\$ 49.6	\$ 10.4	—	—

In addition, we have lines of credit for certain international operations totaling \$32.3 million, of which \$2.8 million was used and \$4.9 million was only available for letters of credit and guarantees, leaving \$24.6 million available to ensure funds are available to meet operating requirements.

In disposing of assets, AWI and some subsidiaries have entered into contracts that included various indemnity provisions, covering such matters as taxes, environmental liabilities and asbestos and other litigation. Some of these contracts have exposure limits, but many do not. Due to the nature of the indemnities, it is not possible to estimate the potential maximum exposure under these contracts. For contracts under which an indemnity claim has been received, a liability of \$5.8 million has been recorded as of December 31, 2008. See Note 32 of the Consolidated Financial Statements for additional information.

#### **RELATED PARTIES**

See Note 31 of the Consolidated Financial Statements for a discussion of our relationship with WAVE.

Related party transactions with executives and outside directors are discussed in Item 13 — Certain Relationships and Related Transactions, and Director Independence.

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

We are exposed to market risk from changes in foreign currency exchange rates, interest rates and commodity prices that could impact our results of operations and financial condition. We use forward swaps and option contracts to hedge currency and commodity exposures. We regularly monitor developments in the capital markets and only enter into currency and commodity transactions with established counterparties having investment-grade ratings. Exposure to individual counterparties is controlled, and thus we consider the risk of counterparty default to be negligible. Forward swap and option contracts are entered into for periods consistent with underlying exposure and do not constitute positions independent of those exposures. We use derivative financial instruments as risk management tools and not for speculative trading purposes. In addition, derivative financial instruments are entered into with a diversified group of major financial institutions in order to manage our exposure to potential nonperformance on such instruments.

Interest Rate Sensitivity

Armstrong is subject to interest rate variability on its Term Loan A, Term Loan B, revolving credit facility and other borrowings. There were no borrowings under the revolving credit facility as of December 31, 2008. A hypothetical increase of one-quarter percentage point in interest rates from December 31, 2008 levels would increase 2009 interest expense by approximately \$1.2 million.

The table below provides information about our long-term debt obligations as of December 31, 2008, including payment requirements and related weighted-average interest rates by scheduled maturity dates. The information is presented in U.S. dollar equivalents, which is our reporting currency.

## Successor Company

## Scheduled maturity date

(\$ millions)	2009	2010	2011	2012	2013	After 2014	Total
As of December 31, 2008							
Long-term debt:							
Fixed rate	\$ 9.9	<\$ 0.1	<\$ 0.1	<\$ 0.1	<\$ 0.1	<\$ 0.1	\$ 10.0
Avg. interest rate	6.19%	5.22%	5.63%	5.63%	5.63%	5.63%	6.19%
Variable rate	\$ 31.0	\$ 32.3	\$ 234.8	\$ 3.5	\$ 184.1	—	\$ 485.7
Avg. interest rate	1.91%	2.04%	2.01%	2.26%	2.26%	—	2.10%

In February 2009 we entered into interest rate swaps with a total notional amount of \$100 million that mature in December 2009. Under the terms of the swaps, we receive 1-month LIBOR and pay a fixed rate over the hedged period. These swaps are designated as cash flow hedges to hedge against changes in LIBOR for a portion of our variable rate debt.

Management's Discussion and Analysis of Financial Condition and Results of Operations  
(dollar amounts in millions)

Exchange Rate Sensitivity

We manufacture and sell our products in a number of countries throughout the world and, as a result, are exposed to movements in foreign currency exchange rates. To a large extent, our global manufacturing and sales provide a natural hedge of foreign currency exchange rate movement. We have used foreign currency forward exchange contracts to reduce our remaining exposure. At December 31, 2008, our major foreign currency exposures are to the Euro, the Canadian dollar and the British pound. A 10% change of all currencies against the U.S. dollar compared to December 31, 2008 levels would impact our 2009 earnings before income taxes by approximately \$3 million, including the impact of current foreign currency forward exchange contracts.

We also use foreign currency forward exchange contracts to hedge exposures created by cross-currency intercompany loans.

The table below details our outstanding currency instruments as of December 31, 2008.

On balance sheet foreign exchange related derivatives

Successor Company

As of December 31, 2008

	Maturing in:		
	2009	2010	Total
Notional amounts (millions)	\$ 120.0	\$ 1.7	\$ 121.7
Assets at fair value (millions)	\$ 7.3	\$ 0.1	\$ 7.4

Commodity Price Sensitivity

We purchase natural gas for use in the manufacture of ceiling tiles and other products, as well as to heat many of our facilities. As a result, we are exposed to movements in the price of natural gas. We have a policy of reducing North American natural gas cost volatility through derivative instruments, including forward swap contracts, purchased call options and zero-cost collars. A 10% increase in North American natural gas prices compared to December 31, 2008 prices would increase our expenses by approximately \$0.9 million. The table below provides information about our natural gas contracts as of December 31, 2008 that are sensitive to changes in commodity prices. Notional amounts are in millions of Btu's ("MMBtu"), while the contract price ranges are shown as the price per MMBtu..

On balance sheet commodity related derivatives

Successor Company

As of December 31, 2008

	Maturing in:		
	2009	2010	Total
Contract amounts (MMBtu)	4,350,000	1,580,000	5,930,000
Contract price range (\$/MMBtu)	\$7.60 – \$13.45	\$6.31 – \$10.40	\$6.31 – \$13.45
Liabilities at fair value (millions)	(\$12.2)	(\$1.3)	(\$13.5)

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

SUPPLEMENTARY DATA

Quarterly Financial Information for the Years Ended December 31, 2008 and 2007 (Unaudited)

The following consolidated financial statements are filed as part of this Annual Report on Form 10-K:

Report of Independent Registered Public Accounting Firm

Consolidated Statements of Earnings for the Years Ended December 31, 2008 (Successor Company) and 2007 (Successor Company), the Three Month Period Ended December 31, 2006 (Successor Company) and the Nine Month Period Ended September 30, 2006 <sup>(1)</sup> (Predecessor Company)

Consolidated Balance Sheets as of December 31, 2008 (Successor Company) and 2007 (Successor Company)

Consolidated Statements of Shareholders' Equity (Deficit) for the Years Ended December 31, 2008 (Successor Company) and 2007 (Successor Company), the Three Month Period Ended December 31, 2006 (Successor Company) and the Nine Month Period Ended September 30, 2006 <sup>(1)</sup> (Predecessor Company)

Consolidated Statements of Cash Flows for the Years Ended December 31, 2008 (Successor Company) and 2007 (Successor Company), the Three Month Period Ended December 31, 2006 (Successor Company) and the Nine Month Period Ended September 30, 2006 <sup>(1)</sup> (Predecessor Company)

Notes to Consolidated Financial Statements

Schedule II for the Years Ended December 31, 2008 (Successor Company) and 2007 (Successor Company), the Three Month Period Ended December 31, 2006 (Successor Company) and the Nine Month Period Ended September 30, 2006 <sup>(1)</sup> (Predecessor Company)

<sup>(1)</sup> The financial statements for the nine month period ended September 30, 2006 include the effects of the Plan of Reorganization and fresh-start reporting in accordance with SOP 90-7 (see Note 3 to the Consolidated Financial Statements).

QUARTERLY FINANCIAL INFORMATION  
ARMSTRONG WORLD INDUSTRIES, INC. (unaudited)

(millions except for per share data)	Successor Company			
	First	Second	Third	Fourth
<b>2008</b>				
Net sales	\$ 828.2	\$ 926.8	\$ 929.6	\$ 708.4
Gross profit	185.9	225.2	211.7	138.2
Net earnings (loss) from continuing operations	15.1	52.4	39.1	(26.2)
Per share of common stock:				
Basic	\$ 0.27	\$ 0.93	\$ 0.69	\$ (0.46)
Diluted	\$ 0.26	\$ 0.91	\$ 0.69	\$ (0.46)
Net earnings (loss)	15.2	52.4	38.9	(25.5)
Per share of common stock:				
Basic	\$ 0.27	\$ 0.93	\$ 0.69	\$ (0.45)
Diluted	\$ 0.27	\$ 0.91	\$ 0.69	\$ (0.45)
Price range of common stock—high	\$ 40.98	\$ 39.44	\$ 40.19	\$ 28.94
Price range of common stock—low	\$ 26.25	\$ 28.92	\$ 27.10	\$ 13.79
Dividends paid per share	\$ 4.50	—	—	—

	Successor Company			
	First	Second	Third	Fourth
<b>2007</b>				
Net sales	\$ 863.4	\$ 920.6	\$ 913.3	\$ 852.4
Gross profit	201.6	233.4	229.2	198.0
Net earnings from continuing operations	30.7	52.7	48.4	21.0
Per share of common stock:				
Basic	\$ 0.55	\$ 0.94	\$ 0.86	\$ 0.37
Diluted	\$ 0.55	\$ 0.93	\$ 0.85	\$ 0.37
Net earnings	26.0	51.6	48.1	19.6
Per share of common stock:				
Basic	\$ 0.47	\$ 0.92	\$ 0.86	\$ 0.35
Diluted	\$ 0.46	\$ 0.91	\$ 0.85	\$ 0.34
Price range of common stock—high	\$ 56.72	\$ 57.48	\$ 52.47	\$ 44.28
Price range of common stock—low	\$ 41.55	\$ 49.85	\$ 35.04	\$ 38.00

There were no dividends paid in 2007.

Note: The net sales and gross profit amounts reported above are reported on a continuing operations basis. The sum of the quarterly earnings per share data may not equal the total year amounts due to changes in the average shares outstanding and, for diluted data, the exclusion of the antidilutive effect in certain quarters.

**Fourth Quarter 2008 Compared With Fourth Quarter 2007**

Net sales of \$708.4 million in the fourth quarter of 2008 decreased from net sales of \$852.4 million in the fourth quarter of 2007, a decrease of 16.9%. Excluding the unfavorable effects of foreign exchange rates of \$27.5 million, net sales decreased 13.8%. Continuing declines in domestic residential markets were exacerbated by escalating weakness in domestic and international commercial markets. Resilient Flooring net sales decreased 10.9%, excluding the unfavorable effects of foreign exchange rates. Volume declines due to broad weakness in residential markets and accelerating declines in commercial markets primarily offset product mix improvement. Wood Flooring net sales decreased by 34.1% primarily due to lower volume driven by continued declines in residential housing markets. Building Products net sales decreased by 2.5%, excluding the unfavorable effects of foreign exchange rates of \$14.6 million. Improved product mix and better price realization offset volume declines across all geographies. Cabinets net sales decreased by 27% on significant volume declines related to further deterioration in the U.S. housing markets. Net sales decreased 18.1% in the Americas. Excluding the unfavorable effects of foreign exchange rates of \$20.9 million, Europe net sales decreased 7.4% and Pacific Rim sales increased 3.3%.

2008 and 2007 operating expenses were impacted by several significant items. The significant items which impacted cost of goods sold ("COGS"), selling, general and administrative expenses ("SG&A") and restructuring charges include:

<b>Increase / (Reduction) in Expenses</b>				
<b>Item</b>	<b>Where Reported</b>	<b>2008</b>	<b>2007</b>	
<b>Fresh-Start: <sup>(1)</sup></b>				
Change in depreciation and amortization	COGS	\$ 1.9	\$	2.1
Impact on hedging-related activity	COGS	—		(1.2)
Change in depreciation and amortization	SG&A	0.3		0.6
<b>Other Significant Items:</b>				
Cost reduction initiatives expenses <sup>(2)</sup>	COGS	4.8		—
Fixed asset impairment <sup>(3)</sup>	COGS	2.9		—
Cost reduction initiatives expenses <sup>(2)</sup>	SG&A	2.3		—
Insurance settlements	SG&A	(6.9)		(5.0)
Environmental accrual	SG&A	—		1.1
Chapter 11 related post-emergence expenses	SG&A	—		0.3
Review of strategic alternatives	SG&A	—		3.8
Intangible asset impairment	Intangible asset impairment	25.4		—

(1) See Note 3 for more information on fresh-start reporting.

(2) See "Factors Affecting Operating Costs" and Notes 15 and 16 for a discussion of the cost reduction expenses.

(3) In 2008 we recorded a fixed asset impairment charge related to certain Resilient Flooring assets.

For the fourth quarter of 2008, the cost of goods sold was 80.5% of net sales, compared to 76.8% in 2007. The 3.7 percentage point increase is primarily due to lower sales to cover fixed costs. The change in the percentages was also impacted by the items detailed in the above table.

SG&A expenses for the fourth quarter of 2008 were \$127.2 million as compared to \$157.8 million for the fourth quarter of 2007. The year-to-year change was primarily due to the factors detailed in the above table offset by a significant decrease in unallocated corporate expense due to lower compensation costs. In addition, most businesses reduced spending in response to lower sales volumes.

During the fourth quarter of 2008, we recorded a non-cash impairment charge of \$25.4 million to reduce the carrying amount of our Wood Flooring trademarks to their estimated fair value based on the results of our annual impairment test. The fair value was negatively affected by lower expected future cash flows due to the decline in the U.S. residential housing market. See Note 12 to the Consolidated Financial Statements for more information.

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Operating loss from continuing operations of \$6.5 million in the fourth quarter of 2008 compared to operating income of \$51.1 million in the fourth quarter of 2007.

Income tax expense from continuing operations for the fourth quarter of 2008 was \$14.6 million on a pre-tax loss of \$11.6 million versus \$26.1 million on pre-tax income of \$47.1 million in 2007. The effective tax rate for the fourth quarter was higher than the comparable 2007 period primarily due to additional valuation allowances on state and foreign deferred income tax assets.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. Our internal control over financial reporting was designed to provide reasonable assurance to management and our Board of Directors regarding the reliability of financial reporting and the fair presentation of our financial statements.

With the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our evaluation, our management concluded that our internal control over financial reporting was effective as of December 31, 2008.

KPMG LLP, an independent registered public accounting firm, audited our internal control over financial reporting. Their audit report can be found on page 57.

/s/ Michael D. Lockhart

Michael D. Lockhart  
Chairman and Chief Executive Officer

/s/ F. Nicholas Grasberger III

F. Nicholas Grasberger III  
Senior Vice President and Chief Financial Officer

/s/ Stephen F. McNamara

Stephen F. McNamara  
Vice President and Corporate Controller



Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders  
Armstrong World Industries, Inc.:

We have audited Armstrong World Industries, Inc. and subsidiaries' ("the Company") internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). 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 conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether 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, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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.

In our opinion, Armstrong World Industries, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements of the Company as listed in the accompanying index on page 52, and our report dated February 25, 2009 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

Philadelphia, Pennsylvania  
February 25, 2009

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders  
Armstrong World Industries, Inc.:

We have audited the consolidated financial statements of Armstrong World Industries, Inc. and subsidiaries (“the Company”) as listed in the accompanying index on page 52. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule as listed in the accompanying index on page 52. These consolidated financial statements and financial statement schedule are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Armstrong World Industries, Inc. and subsidiaries as of December 31, 2008 and 2007 for the Successor Company, and the results of their operations and their cash flows for the years ended December 31, 2008 and 2007 and the three months ended December 31, 2006 for the Successor Company, and for the nine months ended September 30, 2006 for the Predecessor Company, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in Notes 1 and 3 to the consolidated financial statements, on August 18, 2006, the Bankruptcy Court confirmed the Company’s Plan of Reorganization (the Plan), related to its Chapter 11 bankruptcy proceeding. The Plan became effective on October 2, 2006 and Armstrong World Industries, Inc. emerged from the Chapter 11 bankruptcy proceeding. In connection with its emergence from the Chapter 11 bankruptcy proceeding, the Company adopted fresh-start reporting pursuant to Statement of Position 90-7, “Financial Reporting by Entities in Reorganization Under the Bankruptcy Code” as of October 2, 2006. As a result, the financial statements of the Successor Company are presented on a different basis than those of the Predecessor Company and, therefore, are not comparable in all respects. As described in Note 3 to the consolidated financial statements, the Company has reflected the effects of the Plan and fresh-start reporting in the Predecessor Company for the nine month period ended September 30, 2006. As discussed in Note 2 to the consolidated financial statements, upon adoption of fresh-start reporting, the Company adopted FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109” and Statement of Financial Accounting Standards No. 158, “Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106, and 132(R).”

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 25, 2009 expressed an unqualified opinion on the effectiveness of the Company’s internal control over financial reporting.

/s/ KPMG LLP

Philadelphia, Pennsylvania  
February 25, 2009

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Armstrong World Industries, Inc., and Subsidiaries  
Consolidated Statements of Earnings  
(amounts in millions, except per share data)

	Successor Company			Predecessor Company
	Year Ended December 31, 2008	Year Ended December 31, 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006 <sup>(1)</sup>
Net sales	\$ 3,393.0	\$ 3,549.7	\$ 817.3	\$ 2,608.6
Cost of goods sold	2,632.0	2,687.5	660.9	2,030.2
Gross profit	761.0	862.2	156.4	578.4
Selling, general and administrative expenses	579.9	611.3	143.5	415.5
Intangible asset impairment	25.4	—	—	—
Restructuring charges, net	0.8	0.2	1.7	10.0
Equity earnings from joint ventures	(56.0)	(46.0)	(5.3)	(41.4)
Operating income	210.9	296.7	16.5	194.3
Interest expense (unrecorded contractual interest of \$0.0, \$0.0, \$0.0 and \$57.6, respectively)	30.8	55.0	13.4	5.2
Other non-operating expense	1.3	1.4	0.3	1.0
Other non-operating (income)	(10.6)	(18.2)	(4.3)	(7.2)
Chapter 11 reorganization (income), net	—	(0.7)	—	(1,955.5)
Earnings from continuing operations before income taxes	189.4	259.2	7.1	2,150.8
Income tax expense	109.0	106.4	3.8	69.6
Income tax expense on settlement and fresh-start adjustments	—	—	—	657.0
Earnings from continuing operations	80.4	152.8	3.3	1,424.2
Gain (loss) from discontinued operations, net of tax of \$0.4, \$0.3, \$0.9 and \$(8.7), respectively	0.6	(7.5)	(1.1)	(68.4)
Net earnings	<u>\$ 81.0</u>	<u>\$ 145.3</u>	<u>\$ 2.2</u>	<u>\$ 1,355.8</u>
Earnings per share of common stock, continuing operations:				
Basic	\$ 1.43	\$ 2.73	\$ 0.06	n/a
Diluted	\$ 1.42	\$ 2.69	\$ 0.06	n/a
Gain (loss) per share of common stock, discontinued operations:				
Basic	\$ 0.01	\$ (0.13)	\$ (0.02)	n/a
Diluted	\$ 0.01	\$ (0.13)	\$ (0.02)	n/a
Net earnings per share of common stock:				
Basic	\$ 1.44	\$ 2.59	\$ 0.04	n/a
Diluted	\$ 1.43	\$ 2.56	\$ 0.04	n/a
Average number of common shares outstanding:				
Basic	56.4	56.0	55.0	n/a
Diluted	56.6	56.7	55.3	n/a

(1) Reflects the effects of the Plan of Reorganization and fresh-start reporting. See Note 3 to the Consolidated Financial Statements.

See accompanying notes to consolidated financial statements beginning on page 63.



Armstrong World Industries, Inc., and Subsidiaries  
Consolidated Balance Sheets  
(amounts in millions, except share data)

	Successor Company	
	December 31, 2008	December 31, 2007
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 355.0	\$ 514.3
Accounts and notes receivable, net	247.9	300.7
Inventories, net	544.0	543.5
Deferred income taxes	14.4	43.5
Income tax receivable	22.0	25.3
Other current assets	78.2	63.2
Total current assets	1,261.5	1,490.5
Property, plant and equipment, less accumulated depreciation and amortization of \$278.9 and \$158.9, respectively	954.2	1,012.8
Prepaid pension costs	0.3	708.0
Investment in affiliates	208.2	232.6
Intangible assets, net	626.3	686.5
Deferred income taxes	219.6	424.5
Other noncurrent assets	81.7	84.5
Total assets	<u>\$ 3,351.8</u>	<u>\$ 4,639.4</u>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Short-term debt	\$ 1.3	\$ 3.9
Current installments of long-term debt	40.9	24.7
Accounts payable and accrued expenses	337.0	428.2
Income tax payable	1.6	0.5
Deferred income taxes	4.6	29.5
Total current liabilities	385.4	486.8
Long-term debt, less current installments	454.8	485.8
Postretirement and postemployment benefit liabilities	312.8	318.6
Pension benefit liabilities	211.4	205.5
Other long-term liabilities	62.4	67.8
Income taxes payable	164.7	159.4
Deferred income taxes	9.0	471.4
Minority interest in subsidiaries	7.0	6.9
Total noncurrent liabilities	1,222.1	1,715.4
Shareholders' equity:		
Common stock, \$0.01 par value per share, authorized 200 million shares; issued 57,049,495 shares in 2008 and 56,828,754 shares in 2007	0.6	0.6
Capital in excess of par value	2,024.7	2,112.6
Retained earnings	66.7	147.5
Accumulated other comprehensive (loss) income	(347.7)	176.5
Total shareholders' equity	1,744.3	2,437.2
Total liabilities and shareholders' equity	<u>\$ 3,351.8</u>	<u>\$ 4,639.4</u>

See accompanying notes to consolidated financial statements beginning on page 63.



Armstrong World Industries, Inc., and Subsidiaries  
Consolidated Statements of Shareholders' Equity  
(amounts in millions)

	Successor Company				Predecessor Company	
	Year 2008		Year 2007		Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006 <sup>(1)</sup>
<b>Common stock:</b>						
Balance at beginning of period	\$ 0.6		\$ 0.6		\$ 0.6	\$ 51.9
Cancellation of Predecessor common stock	—		—		—	(51.9)
Issuance of Successor common stock	—		—		—	0.6
Balance at end of period	<u>\$ 0.6</u>		<u>\$ 0.6</u>		<u>\$ 0.6</u>	<u>\$ 0.6</u>
<b>Capital in excess of par value:</b>						
Balance at beginning of period	\$ 2,112.6		\$ 2,099.8		\$ 2,097.6	\$ 172.6
Elimination of additional paid in capital due to cancellation of Predecessor common stock	—		—		—	(172.6)
Paid in capital associated with issuance of Successor common stock	—		—		—	2,097.6
Share-based employee compensation	7.2		12.8		2.2	—
Dividends in excess of retained earnings	(95.1)		—		—	—
Balance at end of period	<u>\$ 2,024.7</u>		<u>\$ 2,112.6</u>		<u>\$ 2,099.8</u>	<u>\$ 2,097.6</u>
<b>Reduction for ESOP loan guarantee:</b>						
Balance at beginning of period	\$ —		\$ —		\$ —	\$ (142.2)
Cancellation of Predecessor ESOP loan guarantee	—		—		—	142.2
Balance at end of period	<u>\$ —</u>		<u>\$ —</u>		<u>\$ —</u>	<u>\$ —</u>
<b>Retained earnings (accumulated deficit):</b>						
Balance at beginning of period	\$ 147.5		\$ 2.2		\$ —	\$ (910.8)
Net earnings for period	81.0	\$ 81.0	145.3	\$ 145.3	2.2	\$ 2.2
Dividends	(161.8)		—		—	—
Elimination of Predecessor retained earnings	—		—		—	(445.0)
Balance at end of period	<u>\$ 66.7</u>		<u>\$ 147.5</u>		<u>\$ 2.2</u>	<u>\$ —</u>
<b>Accumulated other comprehensive (loss) income:</b>						
Balance at beginning of period	\$ 176.5		\$ 61.9		\$ —	\$ 37.1
Foreign currency translation adjustments	(42.1)		30.8		1.9	18.5
Derivative gain (loss), net	1.4		(5.4)		0.7	(9.5)
Pension and postretirement adjustments	(483.5)		89.2		59.3	—
Minimum pension liability adjustments	—		—		—	(0.7)
Total other comprehensive (loss) income	<u>(524.2)</u>	<u>(524.2)</u>	<u>114.6</u>	<u>114.6</u>	<u>61.9</u>	<u>61.9</u>
Elimination of Predecessor accumulated other comprehensive income	—		—		—	(45.4)
Balance at end of period	<u>\$ (347.7)</u>		<u>\$ 176.5</u>		<u>\$ 61.9</u>	<u>\$ —</u>
Comprehensive (loss) income	<u>\$ (443.2)</u>		<u>\$ 259.9</u>		<u>\$ 64.1</u>	<u>\$ 1,364.1</u>
<b>Less treasury stock at cost:</b>						
Balance at beginning of period	\$ —		\$ —		\$ —	\$ (528.5)
Elimination of Predecessor treasury stock	—		—		—	528.5
Balance at end of period	<u>\$ —</u>		<u>\$ —</u>		<u>\$ —</u>	<u>\$ —</u>
<b>Total shareholders' equity</b>	<u>\$ 1,744.3</u>		<u>\$ 2,437.2</u>		<u>\$ 2,164.5</u>	<u>\$ 2,098.2</u>

(1) Reflects the effects of the Plan of Reorganization and fresh-start reporting. See Note 3 to the Consolidated Financial Statements.

See accompanying notes to consolidated financial statements beginning on page 63.

Armstrong World Industries, Inc., and Subsidiaries  
Consolidated Statements of Cash Flows  
(amounts in millions)

	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006 <sup>(1)</sup>
<b>Cash flows from operating activities:</b>				
Net earnings	\$ 81.0	\$ 145.3	\$ 2.2	\$ 1,355.8
Adjustments to reconcile net earnings to net cash provided by (used by) operating activities:				
Depreciation and amortization	149.8	137.8	32.2	101.2
Asset impairments	28.3	—	—	0.6
Deferred income taxes	74.0	79.6	1.8	726.2
Share-based compensation	7.5	12.7	2.2	—
Gain on sale of assets	(0.1)	(0.6)	—	(17.1)
Equity earnings from affiliates, net	(56.0)	(46.0)	(5.3)	(41.4)
Distributions from equity affiliates	61.0	117.5	25.0	18.0
U.S. pension credit	(63.0)	(59.4)	(15.7)	(34.3)
Insurance proceeds — environmental recovery	10.0	—	—	—
Asbestos-related insurance recoveries	—	—	—	7.0
Cash effect of hedging activities	2.6	(5.0)	(3.1)	(2.8)
Gain on discharge of debt and liabilities subject to compromise	—	(1.3)	—	(1,510.8)
Non-cash fresh-start adjustments	—	—	—	(389.5)
<b>Changes in operating assets and liabilities:</b>				
Receivables	42.8	29.4	47.4	(66.5)
Inventories	(16.1)	(12.7)	54.8	(12.7)
Other current assets	(7.2)	(7.5)	(5.1)	2.0
Other noncurrent assets	(2.6)	1.2	0.4	(11.0)
Accounts payable and accrued expenses	(88.2)	0.9	(7.0)	20.9
Income taxes payable	9.7	208.6	(4.6)	(64.7)
Other long-term liabilities	(10.2)	(16.6)	(1.8)	(10.5)
Cash distributed under the POR	(3.1)	(14.5)	(28.6)	(804.1)
Other, net	(6.0)	5.8	0.3	5.6
<b>Net cash provided by (used by) operating activities</b>	<b>214.2</b>	<b>575.2</b>	<b>95.1</b>	<b>(728.1)</b>
<b>Cash flows from investing activities:</b>				
Purchases of property, plant and equipment and computer software	(95.0)	(102.6)	(40.3)	(98.2)
Divestitures (acquisitions)	(0.8)	58.8	—	(60.5)
Return of investment from equity affiliate	19.5	—	—	—
Acquisition of equity affiliate	—	(5.2)	—	(4.3)
Loan to affiliate	—	—	—	(6.3)
Proceeds from insurance	—	6.7	—	—
Proceeds from the sale of assets	0.6	5.6	—	39.1
Purchase of minority interest	—	—	—	(1.5)
<b>Net cash (used for) investing activities</b>	<b>(75.7)</b>	<b>(36.7)</b>	<b>(40.3)</b>	<b>(131.7)</b>
<b>Cash flows from financing activities:</b>				
(Decrease)/increase in short-term debt, net	(2.5)	—	2.8	(15.2)
Issuance of long-term debt	5.4	5.0	—	800.0
Payments of long-term debt	(20.9)	(309.2)	(0.2)	(15.5)
Payments under the POR	—	—	—	(300.7)
Debt issuance costs	—	—	(10.7)	—
Financing costs	(2.6)	—	—	—
Special dividend paid	(256.4)	—	—	—
Other, net	—	(1.2)	—	(0.6)



Net cash (used for) provided by financing activities	(277.0)	(305.4)	(8.1)	468.0
Effect of exchange rate changes on cash and cash equivalents	(20.8)	17.4	1.3	5.4
Net (decrease) increase in cash and cash equivalents	\$ (159.3)	\$ 250.5	\$ 48.0	\$ (386.4)
Cash and cash equivalents at beginning of period	\$ 514.3	\$ 263.8	\$ 215.8	\$ 602.2
Cash and cash equivalents at end of period	\$ 355.0	\$ 514.3	\$ 263.8	\$ 215.8
Cash and cash equivalents at end of period from discontinued operations	—	—	11.3	—
Cash and cash equivalents at end of period from continuing operations	\$ 355.0	\$ 514.3	\$ 252.5	\$ 215.8

(1) Reflects the effects of the Plan of Reorganization and fresh-start reporting. See Note 3 to the Consolidated Financial Statements.

See accompanying notes to consolidated financial statements beginning on page 63.

Armstrong World Industries, Inc., and Subsidiaries  
Notes to Consolidated Financial Statements  
(dollar amounts in millions)

NOTE 1. BUSINESS AND CHAPTER 11 REORGANIZATION

Armstrong World Industries, Inc. ("AWI") is a Pennsylvania corporation incorporated in 1891.

On December 6, 2000, AWI filed a voluntary petition for relief ("the Filing") under Chapter 11 of the U.S. Bankruptcy Code ("the Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware ("the Bankruptcy Court") in order to use the court-supervised reorganization process to achieve a resolution of AWI's asbestos-related liability. Also filing under Chapter 11 were two of AWI's wholly-owned subsidiaries, Nitram Liquidators, Inc. ("Nitram") and Desseaux Corporation of North America, Inc. ("Desseaux").

On October 2, 2006, AWI's plan of reorganization ("POR") became effective, and AWI emerged from Chapter 11. The POR excludes AWI's Nitram and Desseaux subsidiaries which pursued separate resolutions of their Chapter 11 cases (see below).

When we refer to "we", "our" and "us" in this report, we are referring to AWI and its subsidiaries. References in this report to "reorganized Armstrong" are to AWI as it was reorganized under the POR on October 2, 2006, and its subsidiaries collectively. We use the term "AWI" when we are referring solely to Armstrong World Industries, Inc.

Resolution of Disputed Claims

All claims in AWI's Chapter 11 case that remained open as of the end of 2007 have been resolved and closed. In February 2008 AWI made a final distribution to general unsecured creditors of AWI under the POR. Distributions were not made for creditors who did not provide required information to AWI. These remaining claimants had until October 24, 2008 to provide the needed information. Some distributions remained unclaimed and, accordingly, AWI recognized a gain of \$0.7 million in the fourth quarter of 2008, which was classified within selling, general and administrative ("SG&A") expenses. The Bankruptcy Court closed AWI's Chapter 11 case on September 2, 2008. No further distributions will be made.

Asbestos PI Trust

On October 2, 2006, the Asbestos PI Trust was created to address AWI's personal injury (including wrongful death) asbestos-related liability. All present and future asbestos-related personal injury claims against AWI, including contribution claims of co-defendants, arising directly or indirectly out of AWI's pre-Filing use of, or other activities involving, asbestos are channeled to the Asbestos PI Trust. See Note 32 under "Asbestos-Related Litigation" for more information on the Asbestos PI Trust.

Matters Concerning AHI

Armstrong Holdings, Inc. ("AHI") was a Pennsylvania corporation and was the publicly held parent holding company of AWI. AHI's only operation was its indirect ownership, through Armstrong Worldwide, Inc. ("AWWD," a Delaware corporation), of all of the capital stock of AWI. Upon AWI's POR becoming effective on October 2, 2006, all then-current shares of AWI were cancelled, and AHI was not entitled to any distribution under the POR in respect of its former equity interest in AWI.

On August 23, 2006, AHI announced that it and AWWD had pending claims in AWI's Chapter 11 case (collectively, the "AHI Claim"). The AHI Claim related to intercompany charges and credits among the companies. During 2007 AHI and AWI reached, and the Bankruptcy Court approved, a settlement on all intercompany claim and tax matters. Under the settlement, AWI paid AHI approximately \$22 million in cash and 98,697 shares of AWI common stock. The settlement gave AWI the right to make all relevant tax elections and file all required tax returns on behalf of the Armstrong group of companies for all relevant tax periods during which the two companies were affiliated, and to receive and retain all related tax refunds.

A final federal income tax return for AHI and AWI on a consolidated basis was filed in September 2007. AHI and AWI reported substantial tax losses in this final joint tax return for these companies. As

Armstrong World Industries, Inc., and Subsidiaries  
Notes to Consolidated Financial Statements  
(dollar amounts in millions)

permitted by its settlement with AHI, AWI chose to carry back its losses for ten years in the return. See Note 17 for further information.

Resolution of Nitram and Desseaux Cases

In September 2007, Nitram and Desseaux proposed a joint plan of liquidation to the Bankruptcy Court. On December 17, 2007, the Bankruptcy Court approved the Joint Amended Plan of Liquidation (the "Joint Plan"). The Joint Plan became effective December 28, 2007. Armstrong contributed \$0.2 million to the estate of Nitram and Desseaux in 2007. Armstrong and its subsidiaries subordinated their claims to those of other unsecured creditors under the Joint Plan and received no distribution from the bankruptcy estate in this case.

Claimants alleging personal injury claims under the Joint Plan are allowed to proceed only against the pre-existing insurance coverage assets of Nitram and will not share in any distribution of general assets.

Deadlines under the Joint Plan for claimants to file claims based on rejected executory contracts or unexpired leases, for administrative claims and for final fee applications passed in January 2008. An initial distribution to unsecured creditors was made in the first quarter of 2008 for the amount of \$0.1 million, and the Bankruptcy Court closed both cases on August 26, 2008. After all the assets in the bankruptcy estate (other than insurance assets available to personal injury claimants) were distributed, Nitram and Desseaux were dissolved. Certificates of Dissolution were filed with the State of Delaware in December 2008.

As a result of the Joint Plan becoming effective on December 28, 2007, Armstrong recorded a \$1.3 million gain from the discharge of liabilities subject to compromise in 2007. The gain was recorded as a Chapter 11 Reorganization activity (see below).

Accounting Impact

AICPA Statement of Position 90-7, "Financial Reporting by Entities in Reorganization under the Bankruptcy Code" ("SOP 90-7") provides financial reporting guidance for entities that are reorganizing under the Bankruptcy Code. This guidance was implemented in the accompanying consolidated financial statements.

SOP 90-7 requires separate reporting of all revenues, expenses, realized gains and losses, and provision for losses related to the Filing as Chapter 11 reorganization costs, net. Accordingly, we recorded the following Chapter 11 reorganization activities during 2007 and 2006. There was no income or expense recorded in 2008.

	<u>Successor Company</u>		<u>Predecessor Company</u>
	<u>Year 2007</u>	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Professional fees	\$ 0.6	\$ —	\$ 30.2
Interest (income)	—	—	(15.0)
(Gain) from discharge of liabilities subject to compromise	(1.3)	—	(1,510.8)
(Gain) from fresh-start reporting	—	—	(459.9)
<b>Total Chapter 11 reorganization (income), net</b>	<b>\$ (0.7)</b>	<b>\$ —</b>	<b>\$ (1,955.5)</b>

Professional fees represent legal and financial advisory fees and expenses that were incurred directly as a result of the Filing. 2007 charges relate to Nitram and Desseaux.

Armstrong World Industries, Inc., and Subsidiaries  
Notes to Consolidated Financial Statements  
(dollar amounts in millions)

Interest income represents income earned from short-term investments between the Filing date and AWI's emergence date.

Pursuant to SOP 90-7, AWI and its subsidiaries adopted fresh-start reporting upon AWI emerging from Chapter 11. The conditions required in order for AWI to adopt fresh-start reporting were met on October 2, 2006. For administrative convenience, we selected September 30, 2006, following the close of business, as the date to adopt fresh-start reporting. Consequently, the impact of emergence, including the gain on settlement of liabilities subject to compromise and the gain on fresh-start reporting, is reflected in the Predecessor Company for the nine months ended September 30, 2006 and the results of operations beginning October 1, 2006 are reflected within the Successor Company. We recorded gains of \$1,510.8 million and \$459.9 million from discharging the liabilities subject to compromise and adopting fresh-start reporting, respectively. See Note 3 for more information on the impact of the implementation of the POR and fresh-start reporting.

AWI recorded \$2.0 million of income for 2008 and incurred \$7.1 million and \$4.6 million of expenses during the year 2007 and the three months ended December 31, 2006, respectively, for Chapter 11 related post-emergence activities. Pursuant to SOP 90-7, these expenses were reported as SG&A expenses.

Reversal of POR-Related Contingent Liability

The POR stipulated that any money received from insurance companies post-emergence for certain environmental matters was owed to the unsecured creditors if the money was received prior to the final distribution being made to the general unsecured creditors. At emergence, we had a \$2.1 million receivable for expected insurance recoveries. We also recorded a \$2.1 million liability to reflect the POR's requirement to pay any received money to the creditors. Since emergence and up to the final distribution date, we had not received any environmental-related money from the insurance companies. With the final distribution made in the first quarter of 2008, we no longer owed any recoveries to the creditors. Accordingly, the \$2.1 million liability was reversed in the first quarter of 2008 as a reduction of SG&A expenses. See Note 32 for further discussion relating to environmental insurance recoveries.

Review of Strategic Alternatives

On February 15, 2007, we announced that we had initiated a review of our strategic alternatives. On February 29, 2008, we announced that we had completed the strategic review process after extensive evaluation of alternatives, including a possible sale of our individual businesses and the entire company. The Board of Directors concluded that it is in the best interest of Armstrong and its shareholders to continue to execute our strategic operating plan under our current structure as a publicly traded company.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation Policy. The consolidated financial statements and accompanying data in this report include the accounts of AWI and its majority-owned subsidiaries. All significant intercompany transactions have been eliminated from the consolidated financial statements.

Use of Estimates. These financial statements are prepared in accordance with U.S. generally accepted accounting principles. The statements include management estimates and judgments, where appropriate. Management utilizes estimates to record many items including asset values, allowances for bad debts, inventory obsolescence and lower of cost or market charges, warranty, workers' compensation, general liability and environmental claims and income taxes. When preparing an estimate, management determines the amount based upon the consideration of relevant information. Management may confer with outside parties, including outside counsel. Actual results may differ from these estimates.

Armstrong World Industries, Inc., and Subsidiaries  
Notes to Consolidated Financial Statements  
(dollar amounts in millions)

Reclassifications. Our policy is to record distributions from equity investments using the equity in earnings method and report returns on investments as cash flows from operating activities. Accordingly, "Distributions from equity affiliates" in the 2006 Consolidated Statements of Cash Flows was reclassified from cash flows from investing activities to cash flows from operating activities. The amounts reclassified were \$25.0 million in the three months ended December 31, 2006 and \$18.0 million for the nine months ended September 30, 2006.

Certain amounts in the Consolidated Statements of Earnings were reclassified from selling, general and administrative expenses to cost of goods sold. The amounts reclassified were \$2.2 million in the year ended December 31, 2007, \$0.5 million in the three months ended December 31, 2006 and \$1.5 million in the nine months ended September 30, 2006.

We also reclassified \$10.5 million in the December 31, 2007 Consolidated Balance Sheet from "Accounts payable and accrued expenses" to "Accounts and notes, receivable, net." This reclassification resulted in a reclassification of \$2.3 in the 2007 Consolidated Statement of Cash Flows from changes in accounts payable and accrued expenses to changes in receivables. Amounts reclassified in the 2006 Consolidated Balance Sheet from "Accounts payable and accrued expenses" to "Accounts and notes receivable, net" resulted in a reclassification of \$2.2 million in the three months ended December 31, 2006 and \$0.5 million in the nine months ended September 30, 2006 in the Consolidated Statement of Cash Flows from changes in accounts payable and accrued expenses to changes in receivables.

Certain other amounts in the prior year's Consolidated Financial Statements and related notes thereto have been recast to conform to the 2008 presentation.

Revenue Recognition. We recognize revenue from the sale of products when persuasive evidence of an arrangement exists, title and risk of loss transfers to the customers, prices are fixed and determinable, and it is reasonably assured the related accounts receivable is collectible. Our sales terms primarily are FOB shipping point. We have some sales terms that are FOB destination. Our products are sold with normal and customary return provisions. Sales discounts are deducted immediately from the sales invoice. Provisions, which are recorded as a reduction of revenue, are made for the estimated cost of rebates, promotional programs and warranties. We defer recognizing revenue if special sales agreements, established at the time of sale, warrant this treatment.

Sales Incentives. Sales incentives are reflected as a reduction of net sales.

Shipping and Handling Costs. Shipping and handling costs are reflected in cost of goods sold.

Advertising Costs. We recognize advertising expenses as they are incurred.

Research and Development Costs. We recognize research and development costs as they are incurred.

Pension and Postretirement Benefits. We have benefit plans that provide for pension, medical and life insurance benefits to certain eligible employees when they retire from active service. Generally, for plans that maintain plan assets, our practice is to fund the actuarially determined current service costs and the amounts necessary to amortize prior service obligations for the pension benefits over periods ranging up to 30 years, but not in excess of the funding limitations.

Taxes. The provision for income taxes has been determined using the asset and liability approach of accounting for income taxes to reflect the expected future tax consequences of events recognized in the financial statements. Deferred income tax assets and liabilities are recognized by applying enacted tax rates to temporary differences that exist as of the balance sheet date which result from differences in the timing of reported taxable income between tax and financial reporting.

Taxes collected from customers and remitted to governmental authorities are reported on a net basis.

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Earnings per Common Share . Basic earnings per share is computed by dividing the earnings by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per common share reflects the potential dilution of securities that could share in the earnings.

Cash and Cash Equivalents . Cash and cash equivalents include cash on hand and short-term investments that have maturities of three months or less when purchased.

Concentration of Credit . We principally sell products to customers in the building products industries in various geographic regions. Net sales to The Home Depot, Inc. were \$285.3 million in the nine months ended September 30, 2006, which is in excess of 10% of our consolidated net sales for that period. Net sales to The Home Depot were less than 10% of consolidated net sales in the years 2008 and 2007 and the three months ended December 31, 2006. Net sales to The Home Depot were recorded in our Resilient Flooring, Wood Flooring and Building Products segments. No other customers accounted for 10% or more of our total consolidated net sales.

There are no significant concentrations of credit risk other than with The Home Depot, Inc. and Lowe's Companies, Inc. who together represented approximately 20% and 23% of our net trade receivables as of December 31, 2008 and 2007, respectively. We monitor the creditworthiness of our customers and generally do not require collateral.

Receivables . We sell the vast majority of our products to select, pre-approved customers using customary trade terms that allow for payment in the future. Customer trade receivables, customer notes receivable and miscellaneous receivables (which include supply related rebates and claims to be received, unpaid insurance claims from litigation and other), net of allowances for doubtful accounts, customer credits and warranties are reported in accounts and notes receivable, net. Notes receivable from divesting certain businesses are included in other current assets and other non-current assets based upon the payment terms.

We establish credit worthiness prior to extending credit. We estimate the recoverability of current and non-current receivables each period. This estimate is based upon triggering events and new information in the period, which can include the review of any available financial statements and forecasts, as well as discussions with legal counsel and the management of the debtor company. As events occur which impact the collectability of the receivable, all or a portion of the receivable is reserved. Account balances are charged off against the allowance when the potential for recovery is considered remote. We do not have any off-balance-sheet credit exposure related to our customers.

Inventories . Inventories are valued at the lower of cost or market. Inventories also include certain samples used in ongoing sales and marketing activities. Cash flows from the sale of inventory and the related cash receipts are classified as operating cash flows on the Consolidated Statements of Cash Flows. See Note 8 for further information on our accounting for inventories.

Property and Depreciation . Property, plant and equipment in place as of September 30, 2006 was set equal to fair value as of our emergence date and are currently stated at that value less accumulated depreciation and amortization. Property, plant and equipment acquired after our emergence date is stated at acquisition cost less accumulated depreciation and amortization.

Depreciation charges for financial reporting purposes are determined on a straight-line basis at rates calculated to provide for the full depreciation of assets at the end of their useful lives. Machinery and equipment includes manufacturing equipment (depreciated over 3 to 15 years), computer equipment (3 to 5 years) and office furniture and equipment (5 to 7 years). Within manufacturing equipment, assets that are subject to quick obsolescence or wear out quickly, such as tooling and engraving equipment, are depreciated over shorter periods (3 to 7 years). Heavy production equipment, such as conveyors and production presses, are depreciated over longer periods (15 years). Buildings are depreciated over 15 to

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30 years, depending on factors such as type of construction and use. Certain buildings existing at our emergence date are depreciated over shorter periods. Computer software is depreciated over 3 to 7 years.

Impairment losses are recorded when indicators of impairment are present, such as operating losses and/or negative cash flows. If an indication of impairment exists, we compare the carrying amount of the asset group to the estimated undiscounted future cash flows expected to be generated by the assets. The amount of impairment loss to be recognized is then measured by comparing the asset group's carrying amount to its fair value. The estimate of an asset group's fair value is based on discounted future cash flows expected to be generated by the asset group, or based on management's estimated exit price assuming the assets could be sold in an orderly transaction between willing parties, or estimated salvage value if no sale is assumed. If the fair value is less than the carrying value of the asset group, we record an impairment charge equal to the difference between the fair value and carrying value of the asset group. Impairments of assets related to our manufacturing operations are recorded in cost of goods sold. When assets are disposed of or retired, their costs and related depreciation are removed from the financial statements and any resulting gains or losses normally are reflected in cost of goods sold or SG&A expenses.

Plant and equipment held under capital leases are stated at the present value of the minimum lease payments. Plant and equipment held under capital leases and leasehold improvements are amortized on a straight line basis over the life of the lease plus any specific option periods.

Asset Retirement Obligations . We recognize the fair value of obligations associated with the retirement of tangible long-lived assets in the period in which they are incurred. Upon initial recognition of a liability, the discounted cost is capitalized as part of the related long-lived asset and depreciated over the corresponding asset's useful life. Over time, accretion of the liability is recognized as an operating expense to reflect the change in the liability's present value.

Intangible Assets . Effective with our emergence from Chapter 11 on October 2, 2006 and as part of fresh-start reporting, Predecessor Company goodwill was eliminated from our balance sheet and intangible assets were revalued. See Note 3 for further information. Intangible assets with determinable useful lives are amortized over their respective estimated useful lives.

We periodically review significant definite-lived intangible assets for impairment under the guidelines of the Financial Accounting Standards Board Statement No. 144 — "Accounting for the Impairment or Disposal of Long-Lived Assets" ("FAS 144"). In accordance with FAS 144, we review our businesses for indicators of impairment such as operating losses and/or negative cash flows. If an indication of impairment exists, we compare the carrying amount of the asset group to the estimated undiscounted future cash flows expected to be generated by the assets. The amount of impairment loss to be recognized is then measured by comparing the asset group's carrying amount to its fair value. The estimate of an asset group's fair value is based on discounted future cash flows expected to be generated by the asset group, or based on management's estimated exit price assuming the assets could be sold in an orderly transaction between willing parties. If the fair value is less than the carrying value of the asset group, we record an impairment charge equal to the difference between the fair value and carrying value of the asset group.

Our indefinite-lived intangibles are primarily trademarks and brand names, which are integral to our corporate identity and expected to contribute indefinitely to our corporate cash flows. Accordingly, they have been assigned an indefinite life. We perform annual impairment tests on these indefinite-lived intangibles under the guidelines of the Financial Accounting Standards Board Statement No. 142 — "Goodwill and Other Intangible Assets" ("FAS 142"). These assets undergo more frequent tests if an indication of possible impairment exists.

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The principal assumptions utilized in our estimates for definite-lived intangible assets include operating profit adjusted for depreciation and amortization and discount rate. The principal assumptions utilized in our estimates for indefinite-lived intangible assets include revenue growth rate, discount rate and royalty rate. Revenue growth rate and operating profit assumptions are consistent with those utilized in our operating plan and long-term financial planning process. The discount rate assumption is calculated based upon an estimated weighted average cost of equity which reflects the overall level of inherent risk and the rate of return an investor would expect to achieve. Methodologies used for valuing our intangible assets did not change from prior periods.

See Note 12 for disclosure on intangible assets.

Foreign Currency Transactions. Assets and liabilities of our subsidiaries operating outside the United States which account in a functional currency other than U.S. dollars are translated using the period end exchange rate. Revenues and expenses are translated at exchange rates effective during each month. Foreign currency translation gains or losses are included as a component of accumulated other comprehensive income (loss) within shareholders' equity. Gains or losses on foreign currency transactions are recognized through the statement of earnings.

Financial Instruments and Derivatives. From time to time, we use derivatives and other financial instruments to offset the effect of currency, interest rate and commodity price variability. See Note 21 for further discussion.

Stock-based Employee Compensation. For awards with only service and performance conditions that have a graded vesting schedule, we recognize compensation expense on a straight-line basis over the vesting period for the entire award. See Note 25 for additional information on stock-based employee compensation.

#### Recently Adopted Accounting Standards

In connection with AWI's emergence from Chapter 11 on October 2, 2006, reorganized Armstrong adopted fresh-start reporting in accordance with AICPA Statement of Position 90-7, "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code" ("SOP 90-7"). As a result of the application of fresh-start reporting in 2006, changes in accounting principles that would have been required in reorganized Armstrong's financial statements within the twelve months following our emergence date were required to be adopted at the time fresh-start reporting was adopted. Accordingly, effective October 2, 2006 we adopted Financial Accounting Standards Board Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes" and Statement of Financial Accounting Standards No. 158 ("FAS 158"), "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans." We adopted no new accounting standards in 2007. In 2008 we adopted the effective provisions of FASB's Statement No. 157 ("FAS 157"), "Fair Value Measurements" and FASB's Emerging Issues Task Force Issue No 06-10 "Accounting for Collateral Assignment Split-Dollar Life Insurance Agreements. See Note 21 for further discussion regarding our adoption of FAS 157.

#### Recently Issued Accounting Standards

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 157 "Fair Value Measurements" ("FAS 157"), which establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. FAS 157 was generally effective for fiscal years beginning after November 15, 2007. However the effective date for certain non-financial assets and liabilities was deferred to fiscal years beginning after November 15, 2008. We do not expect any material impact from adopting the remaining provisions of FAS 157.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 Revised 2007, "Business Combinations" ("FAS 141R"). FAS 141R revises the original FAS 141, while retaining the underlying concept that all business combinations be accounted for at fair value. However, FAS



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141R changes the methodology of applying this concept in that acquisition costs will generally be expensed as incurred, non-controlling interests will be valued at fair value, in-process research and development will be recorded at fair value as an indefinite-lived intangible, restructuring costs associated with a business combination will generally be expensed subsequent to the acquisition and changes in deferred income tax asset allowances after the acquisition date generally will affect income tax expense. This pronouncement applies prospectively to all business combinations whose acquisition dates are on or after the beginning of the first annual period subsequent to December 15, 2008. Additionally, under FAS 141R certain future adjustments to deferred income tax valuation allowances and uncertain tax positions recognized upon our emergence from bankruptcy will impact future earnings.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, "Non-controlling Interests in Consolidated Financial Statements — an amendment of ARB No. 51" ("FAS 160"). FAS 160 requires the recognition of a non-controlling interest (formerly known as a "minority interest") as equity in the consolidated financial statements and separate from the parent's equity. The amount of net income attributable to the non-controlling interest will be included in consolidated net income on the face of the income statement. It also amends certain of ARB 51's consolidation procedures for consistency with the requirements of FAS 141R. This pronouncement is effective for fiscal years, and all interim periods within those fiscal years, beginning after December 15, 2008. Early adoption is not permitted. We do not expect any material impact from adopting FAS 160.

In November 2008 the FASB issued Emerging Issues Task Force No. 08-6 ("EITF 08-6"), "Equity Method Investment Accounting Considerations". EITF 08-6 discusses the accounting for contingent consideration agreements of an equity method investment and the requirement for the investor to recognize its share of any impairment charges recorded by the investee. EITF 08-6 requires the investor to record share issuances by the investee as if it has sold a portion of its investment with any resulting gain or loss being reflected in earnings. EITF 08-6 is effective prospectively for interim periods and fiscal years beginning after December 15, 2008. We do not expect a material impact from the adoption of EITF 08-6.

### NOTE 3. PLAN OF REORGANIZATION AND FRESH-START REPORTING

In connection with its emergence from bankruptcy on October 2, 2006 (the "Effective Date"), AWI adopted fresh-start reporting in accordance with SOP 90-7. For administrative convenience, we selected September 30, 2006, following the close of business, as the date to adopt fresh-start reporting. Consequently, the impact of emergence, including the gain on settlement of liabilities subject to compromise and the gain on fresh-start reporting, is reflected in the Predecessor Company for the nine months ended September 30, 2006 and the results of operations beginning October 1, 2006 are reflected within the Successor Company. Adopting fresh-start reporting resulted in material adjustments to the historical carrying amount of reorganized Armstrong's assets and liabilities. In addition, all accounting standards that were required to be adopted in the financial statements within twelve months following the adoption of fresh-start reporting were adopted as of October 2, 2006. As a result, our post emergence financial statements are not comparable with our pre-emergence financial statements.

In applying fresh-start reporting as of the Effective Date, the reorganization value of reorganized Armstrong was determined to be \$2.94 billion. The approach used to determine reorganized Armstrong's reorganization value, as defined in SOP 90-7, was primarily based on a discounted cash flow approach, while also using a comparable company guideline method as a test for reasonableness of the derived value. These analyses are necessarily based on a variety of estimates and assumptions which, though considered reasonable by management, may not be realized and are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond AWI's control.

Fresh-start reporting required us to allocate this reorganization value to our assets and liabilities based upon their estimated fair values in accordance with procedures specified by Statement of Financial Accounting Standards No. 141, "Business Combinations" ("FAS 141"). Adjustments necessary to state our balance sheet accounts at fair value were made such that the newly assigned fair values of our assets and liabilities fully reflected the emerged entity's reorganization value. No goodwill was assigned

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at emergence. In accordance with FAS 141, we completed our final allocation of reorganization value upon finalization of our analysis of net operating loss carryback alternatives.

In this regard, the initial tax balances for the October 2, 2006 fresh-start balance sheet were calculated assuming that we would elect to carry back our net operating loss ("NOL") two years when filing the 2006 tax returns. During 2007, we continued to evaluate carry back alternatives prior to filing our federal income tax returns in September 2007. Upon completion of this analysis, we decided to file a ten-year carryback. See Note 17 for more information. Since the realizable book value of the NOL based upon a ten-year carryback was different from the calculation based upon a two-year carryback, adjustments to the fresh-start balance sheet were recorded in the third and fourth quarters of 2007 to reflect the ten-year value, as well as for other tax related adjustments.

Collectively, the adjustments described above were re-allocated to other assets and liabilities in 2007 as follows:

Deferred income tax asset — current	\$ 6.8
Property, plant & equipment	54.3
Income tax receivable	7.7
Investment in affiliates	12.6
Other intangibles	28.6
Deferred income tax asset- non current	(89.3)
Total assets	<u>\$ 20.7</u>
Accrued expenses	\$ (0.6)
Income tax payable — current	1.6
Deferred income tax liability — non current	(21.7)
Total liabilities	<u>\$ (20.7)</u>

#### NOTE 4. NATURE OF OPERATIONS

*Resilient Flooring* — produces and sources a broad range of floor coverings primarily for homes and commercial and institutional buildings. Manufactured products in this segment include vinyl sheet, vinyl tile and linoleum flooring. In addition, our Resilient Flooring segment sources and sells laminate flooring products, ceramic tile products, adhesives, installation and maintenance materials and accessories. Resilient Flooring products are offered in a wide variety of types, designs and colors. We sell these products worldwide to wholesalers, large home centers, retailers, contractors and to the manufactured homes industry.

*Wood Flooring* — produces and sources wood flooring products for use in new residential construction and renovation, with some commercial applications in stores, restaurants and high-end offices. The product offering includes pre-finished solid and engineered wood floors in various wood species, and related accessories. Virtually all of our Wood Flooring sales are in North America. Our Wood Flooring products are generally sold to independent wholesale flooring distributors and large home centers. Our products are principally sold under the brand names Bruce<sup>®</sup>, Hartco<sup>®</sup>, Robbins<sup>®</sup>, Timberland<sup>®</sup>, Armstrong<sup>®</sup>, HomerWood<sup>®</sup> and Capella<sup>®</sup>.

*Building Products* — produces suspended mineral fiber, soft fiber and metal ceiling systems for use in commercial, institutional and residential settings. In addition, our Building Products segment sources complementary ceiling products. Our products, which are sold worldwide, are available in numerous colors, performance characteristics and designs, and offer attributes such as acoustical control, rated fire protection and aesthetic appeal. Commercial ceiling materials and accessories are sold to ceiling systems contractors and to resale distributors. Residential ceiling products are sold primarily in North America to wholesalers and retailers (including large home centers). Suspension system (grid) products manufactured by WAVE are sold by both Armstrong and our WAVE joint venture.

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*Cabinets* — produces kitchen and bathroom cabinetry and related products, which are used primarily in the U.S. residential new construction and renovation markets. Through our system of Company-owned and independent distribution centers and through direct sales to builders, our Cabinets segment provides design, fabrication and installation services to single and multi-family homebuilders, remodelers and consumers under the brand names Armstrong® and Bruce®. All of Cabinets' sales are in the U.S.

*Unallocated Corporate* — includes assets, liabilities, income and expenses that have not been allocated to the business units. Balance sheet items classified as Unallocated Corporate are primarily deferred income tax assets, cash and cash equivalents, the Armstrong brand name and the U.S. prepaid pension cost/liability. Expenses for our corporate departments and certain benefit plans are allocated to the reportable segments based on known metrics, such as time reporting, headcount, square-footage or net sales. The remaining items, which cannot be attributed to the reportable segments without a high degree of generalization, are reported in Unallocated Corporate.

Successor Company For the year ended 2008	Resilient Flooring	Wood Flooring	Building Products	Cabinets	Unallocated Corporate	Total
Net sales to external customers	\$ 1,220.1	\$ 624.6	\$ 1,369.1	\$ 179.2	—	\$ 3,393.0
Equity (earnings) from joint ventures	—	—	(56.0)	—	—	(56.0)
Segment operating (loss) income <sup>(1)</sup>	(16.8)	(2.4)	239.7	(6.7)	(2.9)	210.9
Restructuring charges, net of reversals	—	—	—	—	0.8	0.8
Segment assets	670.2	470.9	1,049.6	71.2	1,089.9	3,351.8
Depreciation and amortization	49.8	12.6	64.8	2.4	20.2	149.8
Asset impairments	2.9	25.4	—	—	—	28.3
Investment in affiliates	0.1	—	208.1	—	—	208.2
Capital additions	26.4	11.8	41.1	3.7	12.0	95.0

Successor Company For the year ended 2007	Resilient Flooring	Wood Flooring	Building Products	Cabinets	Unallocated Corporate	Total
Net sales to external customers	\$ 1,230.8	\$ 791.6	\$ 1,292.1	\$ 235.2	—	\$ 3,549.7
Equity loss (earnings) from joint ventures	—	0.6	(46.6)	—	—	(46.0)
Segment operating income (loss) <sup>(1)</sup>	40.4	64.3	221.4	10.5	(39.9)	296.7
Restructuring charges, net of reversals	—	—	0.2	—	—	0.2
Segment assets	734.8	509.7	1,129.2	82.5	2,183.2	4,639.4
Depreciation and amortization	44.0	10.9	59.3	2.6	21.0	137.8
Investment in affiliates	0.1	—	232.5	—	—	232.6
Capital additions	29.9	17.8	37.7	4.4	11.8	101.6

Successor Company For the three months ended December 31, 2006	Resilient Flooring	Wood Flooring	Building Products	Cabinets	Unallocated Corporate	Total
Net sales to external customers	\$ 278.5	\$ 192.6	\$ 289.7	\$ 56.5	—	\$ 817.3
Equity loss (earnings) from joint ventures	—	0.2	(5.5)	—	—	(5.3)
Segment operating income (loss) <sup>(1)</sup>	(1.2)	(0.2)	24.9	0.2	(7.2)	16.5
Restructuring charges, net of reversals	0.3	1.4	—	—	—	1.7
Segment assets	690.1	498.9	1,152.6	81.8	1,729.3	4,152.7
Depreciation and amortization	10.5	2.3	13.9	0.7	4.8	32.2
Investment in affiliates	—	4.0	290.6	—	—	294.6
Capital additions	10.3	10.2	12.1	1.5	4.1	38.2



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Predecessor Company For the nine months ended September 30, 2006	Resilient Flooring	Wood Flooring	Building Products	Cabinets	Unallocated Corporate	Total
Net sales to external customers	\$ 929.4	\$ 645.0	\$ 859.8	\$ 174.4	—	\$ 2,608.6
Equity loss (earnings) from joint ventures	—	0.1	(41.5)	—	—	(41.4)
Segment operating income (loss) <sup>(1)</sup>	12.6	46.2	152.9	6.1	(23.5)	194.3
Restructuring charges, net of reversals	9.6	—	0.5	—	(0.1)	10.0
Depreciation and amortization	35.2	15.0	27.7	2.1	17.8	97.8
Asset impairment	—	0.6	—	—	—	0.6
Capital additions	20.8	23.9	34.1	3.8	10.0	92.6

The table above excludes amounts related to discontinued operations.

- (1) Segment operating income (loss) is the measure of segment profit or loss reviewed by the chief operating decision maker. The sum of the segments' operating income (loss) equals the total consolidated operating income as reported on our income statement. The following reconciles our total consolidated operating income to earnings from continuing operations before income taxes. These items are only measured and managed on a consolidated basis:

	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006 <sup>(1)</sup>
Segment operating income	\$ 210.9	\$ 296.7	\$ 16.5	\$ 194.3
Interest expense	30.8	55.0	13.4	5.2
Other non-operating expense	1.3	1.4	0.3	1.0
Other non-operating (income)	(10.6)	(18.2)	(4.3)	(7.2)
Chapter 11 reorganization (income), net	—	(0.7)	—	(1,955.5)
Earnings from continuing operations before income taxes	<u>\$ 189.4</u>	<u>\$ 259.2</u>	<u>\$ 7.1</u>	<u>\$ 2,150.8</u>

- (1) Reflects the effects of the Plan of Reorganization and fresh-start reporting. See Note 3 to the Consolidated Financial Statements.

Accounting policies of the segments are the same as those described in the summary of significant accounting policies.

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The sales in the table below are allocated to geographic areas based upon the location of the customer.

Geographic Areas	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Net trade sales				
Americas:				
United States	\$ 2,177.4	\$ 2,409.7	\$ 560.7	\$ 1,825.2
Canada	166.0	167.1	36.7	157.6
Other Americas	43.4	38.5	8.8	25.8
Total Americas	<u>\$ 2,386.8</u>	<u>\$ 2,615.3</u>	<u>\$ 606.2</u>	<u>\$ 2,008.6</u>
Europe:				
Germany	\$ 185.7	\$ 164.6	\$ 41.0	\$ 115.6
United Kingdom	134.7	140.4	31.6	94.6
Other Europe	464.1	422.2	91.2	270.3
Total Europe	<u>\$ 784.5</u>	<u>\$ 727.2</u>	<u>\$ 163.8</u>	<u>\$ 480.5</u>
Total Pacific Rim	<u>\$ 221.7</u>	<u>\$ 207.2</u>	<u>\$ 47.3</u>	<u>\$ 119.5</u>
Total net trade sales	<u>\$ 3,393.0</u>	<u>\$ 3,549.7</u>	<u>\$ 817.3</u>	<u>\$ 2,608.6</u>

Long-lived assets (property, plant and equipment), net at December 31	Successor Company	
	2008	2007
Americas:		
United States	\$ 709.9	\$ 747.0
Other Americas	14.7	21.2
Total Americas	<u>\$ 724.6</u>	<u>\$ 768.2</u>
Europe:		
Germany	\$ 112.0	\$ 108.7
Other Europe	68.6	85.0
Total Europe	<u>\$ 180.6</u>	<u>\$ 193.7</u>
Total Pacific Rim	<u>\$ 49.0</u>	<u>\$ 50.9</u>
Total long-lived assets, net	<u>\$ 954.2</u>	<u>\$ 1,012.8</u>

#### NOTE 5. ACQUISITIONS

On April 3, 2006 we purchased certain assets and assumed certain liabilities of HomerWood, Inc., a hardwood flooring company. On May 1, 2006 we purchased certain assets and assumed certain liabilities of Capella Engineered Wood, LLC, a hardwood flooring company, and of its parent company, Capella, Inc. The combined purchase price of these acquisitions was \$61.5 million. Both acquisitions were financed from existing cash balances. Both investments expanded Armstrong's wood flooring product offerings. The acquisitions were accounted for under the purchase method of accounting in the second quarter of 2006.

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On August 20, 2007 we purchased the remaining 50% interest in Kunshan Holding Limited for \$5.2 million, at which time it became a wholly-owned subsidiary. The acquisition was accounted for under the purchase method of accounting during the third quarter of 2007.

On February 18, 2008 we acquired the assets of Bowmans Australia Pty Ltd. to complement our Australian Building Products business for total consideration of \$0.8 million.

The allocation of the purchase price to the fair value of tangible and identifiable intangible assets acquired in each of these acquisitions has been completed.

**NOTE 6. DISCONTINUED OPERATIONS**

On May 31, 2000 Armstrong completed its sale of all entities, assets and certain liabilities comprising its Insulation Products segment. During the fourth quarter of 2006, we recorded a net gain of \$1.7 million due to the settlement of various legal disputes. During the first quarter of 2008, we recorded a gain of \$1.0 million (\$0.6 million net of income tax) arising from the settlement of a legal dispute. In accordance with Financial Accounting Standards Board ("FASB") Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("FAS 144"), these adjustments were classified as discontinued operations since the original divestiture was reported as discontinued operations.

On March 27, 2007 we entered into an agreement to sell Tapijtfabriek H. Desseaux N.V. and its subsidiaries — the principal operating companies in our European Textile and Sports Flooring business. These companies were first classified as discontinued operations at October 2, 2006 when they met the criteria of FAS 144. The sale transaction was completed in April 2007 and total proceeds of \$58.8 million were received during 2007. Certain post completion adjustments specified in the agreement were disputed by the parties after the sale. The matter was referred to an independent expert for a final and binding determination. On December 30, 2008 a final decision was reached with all disputed items awarded in our favor. The disputed amount was recorded as a receivable since April 2007 with the interest receivable recorded in December 2008 (included as part of 'Other current assets'). Full payment of \$8.0 million was received in January 2009.

During 2008 we incurred post completion expenses which were offset by the interest income recorded in the fourth quarter of 2008.

Prior period results within the Consolidated Statement of Earnings have been recast to reflect the results of discontinued operations. The segment results in Note 4 exclude the amounts related to discontinued operations. The Consolidated Statements of Cash Flows do not separately report the cash flows of the discontinued operations, as these cash flows were not material to any cash flow category.

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Net sales, pre-tax loss and net loss from discontinued operations of Tapijtfabriek H. Desseaux N.V. and its subsidiaries are as follows:

	Successor Company		Predecessor Company	
	Year 2008	Year 2007	Three Months Ended December 30, 2006	Nine Months Ended September 30, 2006 <sup>(1)</sup>
Net sales	\$ —	\$ 59.8	\$ 66.7	\$ 187.1
Pre-tax loss from discontinued operations	\$ —	\$ (1.4)	\$ (2.8)	\$ (6.7)
Fresh-start reporting adjustments	—	—	—	(70.4)
(Loss) gain on expected disposal of discontinued operations	—	(5.8)	2.6	—
Income tax (expense) benefit	—	(0.3)	(0.9)	8.7
Net (loss) from discontinued operations	<u>\$ —</u>	<u>\$ (7.5)</u>	<u>\$ (1.1)</u>	<u>\$ (68.4)</u>

(1) Reflects the effects of fresh-start reporting.

NOTE 7. ACCOUNTS AND NOTES RECEIVABLE

	Successor Company	
	December 31, 2008	December 31, 2007
Customer receivables	\$ 287.1	\$ 342.2
Customer notes	6.7	7.6
Miscellaneous receivables	8.6	14.6
Less allowance for discounts and losses	(54.5)	(63.7)
Net accounts and notes receivable	<u>\$ 247.9</u>	<u>\$ 300.7</u>

The decrease in accounts and notes receivable is primarily due to lower sales in November and December 2008 as compared to the comparable periods of 2007.

Generally, we sell our products to select, pre-approved customers whose businesses are affected by changes in economic and market conditions. We consider these factors and the financial condition of each customer when establishing our allowance for losses from doubtful accounts.



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**NOTE 8. INVENTORIES**

Following are the components of our inventories:

	Successor Company	
	December 31, 2008	December 31, 2007
Finished goods	\$ 371.2	\$ 355.7
Goods in process	39.6	39.7
Raw materials and supplies	152.7	160.7
Less LIFO and other reserves	(19.5)	(12.6)
Total inventories, net	<u>\$ 544.0</u>	<u>\$ 543.5</u>

Approximately 63% and 65% of our total inventory in 2008 and 2007, respectively, was valued on a LIFO (last-in, first-out) basis. Inventory values were lower than would have been reported on a total FIFO (first-in, first-out) basis by \$8.9 million and \$2.4 million at the end of 2008 and 2007, respectively.

The distinction between the use of different methods of inventory valuation is primarily based on geographical locations and/or legal entities rather than types of inventory. The following table summarizes the amount of inventory that is not accounted for under the LIFO method.

	Successor Company	
	2008	2007
International locations	\$ 171.3	\$ 158.8
Cabinets	22.3	27.3
Wood flooring	1.3	1.0
Resilient flooring	1.0	1.1
U.S. sourced products	3.4	2.5
Total	<u>\$ 199.3</u>	<u>\$ 190.7</u>

Substantially all of our international locations use the FIFO method of inventory valuation (or other methods which closely approximate the FIFO method) primarily because either the LIFO method is not permitted for local tax and/or statutory reporting purposes, or the entities were part of various acquisitions that had adopted the FIFO method prior to our acquisition. In these situations, a conversion to LIFO would be highly complex and involve excessive cost and effort to achieve under local tax and/or statutory reporting requirements.

The sourced products represent certain finished goods sourced from third party manufacturers, primarily from foreign suppliers.

**NOTE 9. OTHER CURRENT ASSETS**

	Successor Company	
	December 31, 2008	December 31, 2007
Prepaid expenses	\$ 34.5	\$ 36.4
Fair value of derivative asset	11.7	0.8
Receivable related to discontinued operations	8.0	7.8
Assets held for sale	7.8	7.9
Other	16.2	10.3
Total other current assets	<u>\$ 78.2</u>	<u>\$ 63.2</u>

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NOTE 10. PROPERTY, PLANT AND EQUIPMENT

	Successor Company	
	December 31, 2008	December 31, 2007
Land	\$ 129.0	\$ 131.7
Buildings	296.5	287.6
Machinery and equipment	722.8	664.6
Computer software	36.2	36.2
Construction in progress	48.6	51.6
Less accumulated depreciation and amortization	(278.9)	(158.9)
Net property, plant and equipment	<u>\$ 954.2</u>	<u>\$ 1,012.8</u>

Pursuant to SOP 90-7 upon adopting fresh-start reporting in 2006 we recorded a \$242.6 million reduction to reflect the fair value of our net property, plant and equipment. In the third and fourth quarters of 2007, we recorded additional adjustments to increase the estimated fair value of net property, plant and equipment on our October 2, 2006 fresh-start balance sheet by \$54.3 million (\$48.8 million to machinery and equipment and \$5.5 million to land). See Note 3 for further information.

See Note 2 for discussion of policies related to property and depreciation and asset retirement obligations.

NOTE 11. EQUITY INVESTMENTS

Investments in affiliates of \$208.2 million at December 31, 2008 reflected the equity interest in our 50% investment in our WAVE joint venture.

On August 20, 2007 we purchased the remaining 50% interest in Kunshan Holding Limited ("Kunshan") for \$5.2 million, at which time it became a wholly-owned subsidiary. Our equity investment in Kunshan at December 31, 2006 of \$4.0 million along with our additional investments was reclassified as part of the purchase accounting for the subsidiary.

The decrease in the investment balance from December 31, 2007 of \$24.4 million is due to distributions from WAVE of \$80.5 million (including a special distribution of \$25.0 million in December 2008), partially offset by our equity interest in WAVE's earnings. We use the equity in earnings method to determine the appropriate classification of these distributions within our Consolidated Statements of Cash Flows. During 2008 WAVE distributed amounts in excess of our capital contributions and proportionate share of retained earnings. Accordingly, \$19.5 million of the distributions were reflected as a return of investment in cash flows from investing activity in our Consolidated Statement of Cash Flows. The remaining \$61.0 million was recorded within cash flows from operating activities.

Affiliate	Income Statement Classification	Successor Company			Predecessor Company
		Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
WAVE	Equity earnings from joint venture	\$ 56.0	\$ 46.6	\$ 5.5	\$ 41.5
Kunshan	Equity loss from joint venture	—	(0.6)	(0.2)	(0.1)

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We account for our WAVE joint venture using the equity method of accounting. Our recorded investment in WAVE was higher than our 50% share of the carrying values reported in WAVE's consolidated financial statements by \$213.0 million as of December 31, 2008 and \$219.7 million as of December 31, 2007. These differences are due to our adopting fresh-start reporting upon emerging from Chapter 11, while WAVE's consolidated financial statements do not reflect fresh-start reporting. The differences are comprised of the following fair value adjustments to assets:

	December 31, 2008	December 31, 2007
Property, plant and equipment	\$ 2.8	\$ 3.9
Other intangibles	179.7	185.3
Goodwill	30.5	30.5
Total	<u>\$ 213.0</u>	<u>\$ 219.7</u>

Other intangibles include customer relationships, trademarks and developed technology. Customer relationships are amortized over 20 years and developed technology is amortized over 15 years. Trademarks have an indefinite life.

See Exhibit 99 for WAVE's consolidated financial statements. Condensed financial data for WAVE is summarized below:

	December 31, 2008	December 31, 2007
Current assets	\$ 132.5	\$ 131.0
Non-current assets	32.8	30.9
Current liabilities	21.6	28.9
Other non-current liabilities	156.8	104.1

	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Net sales	\$ 421.8	\$ 380.0	\$ 88.6	\$ 260.2
Gross profit	160.2	134.9	21.3	102.8
Net earnings	125.4	107.0	21.9	83.0

See discussion in Note 31 for additional information on this related party.

#### NOTE 12. INTANGIBLE ASSETS

Pursuant to SOP 90-7 we recorded the estimated fair value of intangibles, not including goodwill, of \$673.6 million upon adopting fresh-start reporting. In the third and fourth quarters of 2007, we recorded additional adjustments to increase the estimated fair value of intangibles, not including goodwill, by \$28.6 million (\$16.6 million to trademarks, \$8.2 million to customer relationships and \$3.8 million to developed technology). See Note 3 for a discussion of these adjustments.

During the fourth quarter of 2008, we completed our annual impairment analysis as required by Financial Accounting Standards Board Statement No. 142 — "Goodwill and Other Intangible Assets" ("FAS 142"). We determined that the carrying value of our Wood Flooring trademarks was in excess of their fair value, due to lower sales caused by the decline in the U.S. residential housing market. We determined the fair value of these intangible assets by utilizing a discounted cash flow analysis that incorporated projections of revenue and cash flows. Based on the result of the analysis, we recorded a non-cash impairment charge of \$25.4 million in the fourth quarter of 2008. See Note 2 for a discussion of our accounting policy for intangible assets.

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Further adjustments were made to the carrying value of intangibles during the fourth quarter of 2008. These adjustments were primarily tax-related.

The following table details amounts related to our intangible assets as of December 31, 2008 and 2007.

	Estimated Useful Life	Successor Company			
		December 31, 2008		December 31, 2007	
		Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
<b>Amortizing intangible assets</b>					
Customer relationships	20 years	\$ 171.4	\$ 19.2	\$ 173.3	\$ 10.5
Developed technology	15 years	81.0	12.0	81.7	6.6
Other	Various	9.5	0.3	12.4	1.1
<b>Total</b>		<b>\$ 261.9</b>	<b>\$ 31.5</b>	<b>\$ 267.4</b>	<b>\$ 18.2</b>
<b>Non-amortizing intangible assets</b>					
Trademarks and brand names	Indefinite	395.9		437.3	
<b>Total other intangible assets</b>		<b>\$ 657.8</b>		<b>\$ 704.7</b>	

**Aggregate Amortization Expense and Impairment Charges**

Successor Company

For the year ended December 31, 2008	\$ 39.7
Amortization	14.3
Intangible asset impairment	25.4
For the year ended December 31, 2007	14.5
Amortization	14.5
Intangible asset impairment	—

The annual amortization expense expected for the years 2009 through 2013 is as follows:

2009	\$ 14.1
2010	14.1
2011	14.1
2012	14.1
2013	14.1

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NOTE 13. OTHER NON-CURRENT ASSETS

	Successor Company	
	December 31, 2008	December 31, 2007
Cash surrender value of Company owned life insurance policies	\$ 53.5	\$ 52.9
Other	28.2	31.6
Total other non-current assets	<u>\$ 81.7</u>	<u>\$ 84.5</u>

NOTE 14. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

	Successor Company	
	December 31, 2008	December 31, 2007
Payables, trade and other	\$ 179.3	\$ 231.2
Employment costs	107.1	130.7
Other	50.6	66.3
Total accounts payable and accrued expenses	<u>\$ 337.0</u>	<u>\$ 428.2</u>

The decrease in accounts payable and accrued expenses is primarily due to a reduction in trade payables due to lower activity and lower accruals for employee incentive compensation.

NOTE 15. SEVERANCES AND RELATED COSTS

In 2008 we recorded \$7.4 million of severance and related expenses to reflect the termination costs for certain corporate employees. We also recorded a reduction of our stock compensation expense of \$1.5 million in the first quarter of 2008 related to stock grants that were forfeited by these employees. These costs were recorded as SG&A expenses.

During 2008 we recorded \$14.1 million of severance and other related charges primarily related to organizational and manufacturing changes for our European resilient flooring business. The organizational changes are due to the decision to consolidate and outsource several SG&A functions. The manufacturing changes related primarily to the decision to cease production of automotive carpeting and other specialized textile flooring products. These charges were recorded as part of cost of goods sold (\$7.3 million) and SG&A expenses (\$6.8 million). None of the severance payments were made as of December 31, 2008.

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**NOTE 16. RESTRUCTURING AND OTHER ACTIONS**

Net restructuring charges of \$0.8 million, \$0.2 million, \$1.7 million and \$10.0 million were recorded in the year 2008, the year 2007, the three months ended December 31, 2006 and the nine months ended September 30, 2006, respectively. The following table summarizes these charges:

Action Title	Successor Company		Predecessor Company		(unaudited) Number of Employees Impacted	Segment
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006		
Lancaster Plant	—	—	\$ 0.5	\$ 9.6	450	Resilient Flooring
Other initiatives	\$ 0.8	\$ 0.2	1.2	0.4		Various
<b>Total</b>	<b>\$ 0.8</b>	<b>\$ 0.2</b>	<b>\$ 1.7</b>	<b>\$ 10.0</b>		

Lancaster Plant: These charges related to the fourth quarter 2004 decision to cease commercial flooring production at Lancaster, Pennsylvania in 2006. We made this decision because of changes in the level and structure of demand for vinyl flooring products, we had excess capacity in other plants and Lancaster was our highest cost plant. Commercial flooring production requirements are being serviced in part by our other facilities around the world. We recorded no costs in 2008 or 2007 related to this initiative, but recorded the following costs in 2006:

	Successor Company	Predecessor Company
	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Non-cash restructuring charges for enhanced retirement benefits	\$ 0.5	\$ 8.5
Severance and related costs	—	1.1
<b>Total restructuring charges</b>	<b>\$ 0.5</b>	<b>\$ 9.6</b>
Accelerated depreciation	—	\$ 0.3
Other related costs	\$ 0.5	9.3
<b>Total cost of goods sold</b>	<b>\$ 0.5</b>	<b>\$ 9.6</b>
Gain on sale of warehouse	—	\$ (14.3)
Other related costs	—	7.4
<b>Total SG&amp;A expenses</b>	<b>—</b>	<b>\$ (6.9)</b>

Other related costs recorded in cost of goods sold related primarily to commercial flooring site clean-up and maintenance costs and costs to redesign the remaining portions of the plant to function without the commercial flooring site. Other related costs in SG&A expenses primarily related to the donation of the commercial flooring site to an outside party.

We have incurred project-to-date restructuring charges of \$27.4 million related to costs for enhanced retirement benefits (\$23.7 million) and severance and related employee costs (\$3.7 million). We do not expect to incur any additional restructuring or other charges related to this initiative in the future.

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The following table summarizes activity in the restructuring accruals for 2007 and 2008. Net charges in the table may not agree with the income statement due to non-cash charges for enhanced retirement benefits that did not affect the restructuring accrual amounts.

Successor Company:	Severance and Related Costs		Leases	Total
	Lancaster Plant	Other Initiatives	U.K. Lease	
December 31, 2006	\$ 0.4	\$ 1.7	\$ 4.9	\$ 7.0
Cash payments	(0.4)	(1.8)	(0.5)	(2.7)
Net charges	—	0.2	—	0.2
Other	—	—	0.1	0.1
December 31, 2007	\$ —	\$ 0.1	\$ 4.5	\$ 4.6
Cash payments	—	—	(0.7)	(0.7)
Net charges	—	—	0.8	0.8
Other	—	(0.1)	(1.2)	(1.3)
December 31, 2008	\$ —	\$ —	\$ 3.4	\$ 3.4

The amounts in "Other" are related to the effects of foreign currency translation.

The remaining balance of \$3.4 million as of December 31, 2008 relates to a noncancelable U.K. operating lease, which extends through 2017.

#### NOTE 17. INCOME TAXES

The tax effects of principal temporary differences between the carrying amounts of assets and liabilities and their tax bases are summarized in the table below. Management believes it is more likely than not that results of future operations will generate sufficient taxable income to realize deferred tax assets, net of valuation allowances, including the remaining federal net operating losses of \$357.6 million principally resulting from payments to the Asbestos PI Trust in 2006 under the POR that may be carried forward for the remaining 18 years. In arriving at this conclusion, we considered the profit before tax generated for the years 1996 through 2008, as well as future reversals of existing taxable temporary differences and projections of future profit before tax.

We have provided valuation allowances for certain deferred state and foreign income tax assets, foreign tax credits and other basis adjustments of \$208.7 million. We have \$1,404.2 million of state net operating loss carryforwards with expirations between 2009 and 2028, and \$393.7 million of foreign net operating loss carryforwards, that are available for carryforward indefinitely.

Our valuation allowances decreased from 2007 by a net amount of \$16.3 million. This includes a decrease of \$35.9 million for foreign tax credits and capital loss carryforwards, an increase for certain deferred state income tax assets of \$15.2 million, and an increase for foreign tax loss carryforwards of \$4.4 million. The decrease in the foreign tax credits was primarily due to the expiration of prior foreign tax credits. The increase in the valuation allowance for certain deferred state income tax assets of \$15.2 million was primarily due to a reduction in the amount of future reversals of existing taxable temporary differences. The increase in the valuation allowance for foreign tax loss carryforwards was primarily due to additional unbenefitted losses partially offset by foreign currency translation adjustments that also reduced the related deferred income tax assets. We estimate we will need to generate future taxable income of approximately \$1,021.8 million for federal income tax purposes and \$1,165.4 million for state income tax purposes in order to fully realize the net deferred income tax assets discussed above.

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	Successor Company	
	December 31, 2008	December 31, 2007
Deferred income tax assets (liabilities)		
Postretirement and postemployment benefits	\$ 170.4	\$ 169.1
Pension benefit liabilities	32.2	21.5
Net operating losses	529.8	573.8
Foreign tax credit carryforwards	70.7	105.3
Capital losses	15.2	16.7
Other	82.3	86.3
Total deferred income tax assets	900.6	972.7
Valuation allowances	(208.7)	(225.0)
Net deferred income tax assets	691.9	747.7
Intangibles	(289.7)	(316.3)
Accumulated depreciation	(102.2)	(117.6)
Prepaid pension costs	—	(268.4)
Tax on unremitted earnings	(48.7)	(51.0)
Inventories	(18.9)	(20.6)
Other	(12.0)	(6.7)
Total deferred income tax liabilities	(471.5)	(780.6)
Net deferred income tax assets (liabilities)	\$ 220.4	\$ (32.9)

Deferred income taxes have been classified in the Consolidated Balance Sheet as:

Deferred income tax assets — current	\$ 14.4	\$ 43.5
Deferred income tax assets — noncurrent	219.6	424.5
Deferred income tax liabilities — current	(4.6)	(29.5)
Deferred income tax liabilities — noncurrent	(9.0)	(471.4)
Net deferred income tax assets (liabilities)	\$ 220.4	\$ (32.9)



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Details of taxes	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Earnings from continuing operations before income taxes:				
Domestic	\$ 171.0	\$ 221.4	\$ 34.0	\$ 1,950.1
Foreign	18.4	42.1	(6.4)	196.0
Eliminations	—	(4.3)	(20.5)	4.7
<b>Total</b>	<b>\$ 189.4</b>	<b>\$ 259.2</b>	<b>\$ 7.1</b>	<b>\$ 2,150.8</b>
Income tax provision (benefit):				
Current:				
Federal	\$ 8.3	\$ 4.8	—	\$ (13.2)
Foreign	21.3	17.4	\$ 1.8	14.6
State	5.4	4.6	0.2	(1.0)
<b>Total current</b>	<b>35.0</b>	<b>26.8</b>	<b>2.0</b>	<b>0.4</b>
Deferred:				
Federal	46.5	72.5	3.7	761.6
Foreign	(1.1)	1.5	(1.7)	(6.2)
State	28.6	5.6	(0.2)	(29.2)
<b>Total deferred</b>	<b>74.0</b>	<b>79.6</b>	<b>1.8</b>	<b>726.2</b>
<b>Total income taxes</b>	<b>\$ 109.0</b>	<b>\$ 106.4</b>	<b>\$ 3.8</b>	<b>\$ 726.6</b>

At December 31, 2008, we had \$137.5 million of book basis (including unremitted earnings) in excess of tax basis in the shares of certain foreign subsidiaries for which no deferred income taxes have been provided because we consider the underlying earnings to be permanently reinvested. This basis difference could reverse through a sale of the subsidiaries, the receipt of dividends from the subsidiaries, as well as various other events. It is not practical to calculate the residual income tax which would result if these basis differences reversed due to the complexities of the tax law and the hypothetical nature of the calculations. We do, however, estimate that approximately \$2.0 million in foreign withholding taxes would be payable if the underlying earnings were to be distributed.

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	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Reconciliation to U.S. statutory tax rate				
Continuing operations tax at statutory rate	\$ 66.3	\$ 90.7	\$ 2.5	\$ 752.8
State income taxes (benefit), net of federal benefit	8.1	6.7	—	(30.2)
Increases in valuation allowances on deferred state income tax assets	13.9	—	—	—
Increases in valuation allowances on deferred foreign income tax assets	14.2	6.0	4.8	35.7
Tax on foreign and foreign-source income	(0.9)	(1.7)	(5.0)	(1.1)
Bankruptcy reorganization expenses	—	0.4	2.0	8.8
Interest on uncertain tax positions	5.9	1.8	—	—
Permanent book/tax differences	(2.4)	(0.4)	(0.8)	(25.8)
Permanent fresh-start adjustments	—	—	—	(0.9)
Permanent settlement adjustments	—	—	—	(39.6)
Tax on unremitted earnings	3.9	2.9	0.3	26.9
	<u>\$ 109.0</u>	<u>\$ 106.4</u>	<u>\$ 3.8</u>	<u>\$ 726.6</u>
Tax expense at effective rate				

The effective tax rate for the year ended December 31, 2007 includes a benefit of \$5.0 million (net of federal benefit) for legislative changes in New York and Texas and \$1.0 million for the reduction in the German income tax rate.

As previously described, we funded the Asbestos PI Trust in 2006 resulting in certain significant tax adjustments that impacted the effective tax rate for the nine months ended September 30, 2006. We reduced valuation allowances of approximately \$29.2 million related to certain state net operating losses and deferred income tax assets as available evidence, including pre-tax profit projections and new deferred tax liabilities on fresh-start adjustments, indicated that it is more likely than not that these benefits will be realized. In addition, as part of fresh-start reporting, several significant balance sheet accounts were adjusted resulting in a permanent book versus tax difference which had an impact on the effective tax rate. These adjustments were primarily the reduction in the carrying value of nondeductible goodwill as well as certain other foreign currency translation accounts.

The effective tax rate for the three months ended December 31, 2006, reflects a tax benefit of \$1.5 million related to a change in German tax law that allows for a recovery of previously frozen imputation tax credits. This benefit was more than offset, however, by foreign losses incurred during the quarter for which a full valuation allowance is required.

In accordance with the requirements for fresh-start reporting pursuant to SOP 90-7, we adopted FIN 48 effective as of October 2, 2006. The transition adjustments, although not material in the aggregate, were shown as an adjustment to the October 2, 2006 fresh-start balance sheet.

We have \$174.4 million of Unrecognized Tax Benefits ("UTB") as of December 31, 2008. Of this amount, \$160.0 million, if recognized in future periods, would impact the reported effective tax rate. The remaining amount of \$14.4 million, if recognized in future periods, would be fully reduced by additional valuation allowances.

In October 2007 we received \$178.7 million in refunds for federal income taxes paid over the preceding ten years. The refunds result from the carryback of a portion of net operating losses created by the funding of the Asbestos PI Trust in October 2006. The tax refunds are subject to examination and

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adjustment by the Internal Revenue Service ("IRS") under its normal audit procedures. Upon receipt of the refunds, AWI recorded a liability of \$144.6 million in the fourth quarter of 2007 pending completion of the IRS audit. Any tax losses disallowed for a ten-year carryback would be available to carry forward. This amount is included in the table of UTB's below.

It is reasonably possible that certain UTB's may increase or decrease within the next twelve months due to tax examination changes, settlement activities, expirations of statute of limitations, or the impact on recognition and measurement considerations related to the results of published tax cases or other similar activities. Over the next twelve months, we estimate that UTB's may decrease by \$0.3 million due to statutes expiring and increase by \$1.7 million due to uncertain tax positions expected to be taken on tax returns.

With our adoption of FIN 48, we elected to continue our prior practice of accounting for all interest and penalties on uncertain income tax positions as income tax expense. As a result, we have reported \$10.0 million of interest and penalty exposure as accrued income tax in the Consolidated Balance Sheet as of December 31, 2008, of which \$6.4 million was recognized as income tax during 2008.

We have significant operations in over 26 countries and file income tax returns in approximately 80 tax jurisdictions, in some cases for multiple legal entities per jurisdiction. Generally, we have open tax years subject to tax audit scrutiny on average of between three years and six years. We have not materially extended any open statutes of limitation for any significant location and have reviewed and accrued for, where necessary, tax liabilities for open periods. We are currently under examination by the IRS for the 2005 and 2006 tax years. In addition to those years, the tax years 2007 and 2008 are subject to future potential tax adjustments. All tax years prior to 2005 have been settled. We also have examinations in progress in Germany and Canada. We have evaluated the need for tax reserves for these audits as part of our FIN 48 evaluation process.

We had the following activity for UTB's for the year ended December 31, 2008:

	Non-Current Income Taxes Payable	NOL Carryforward	Total
Unrecognized tax benefits at December 31, 2007	\$ 13.6	\$ 167.1	\$ 180.7
Gross change for current year positions	0.8	—	0.8
Increases for prior period positions	0.4	3.0	3.4
Decrease for prior period positions	—	(8.0)	(8.0)
Decrease due to settlements and payments	(0.9)	—	(0.9)
Decrease due to statute expirations	(1.6)	—	(1.6)
Unrecognized tax benefits at December 31, 2008	<u>\$ 12.3</u>	<u>\$ 162.1</u>	<u>\$ 174.4</u>

	Successor Company		Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006
Other taxes			Nine Months Ended September 30, 2006
Payroll taxes	\$ 75.6	\$ 77.1	\$ 16.9
Property, franchise and capital stock taxes	15.4	18.3	4.6

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## NOTE 18. DEBT

	Successor Company			
	2008	Average year-end interest rate	2007	Average year-end interest rate
Term Loan A due 2011	\$ 281.3	2.01%	\$ 296.3	6.22%
Term Loan B due 2013	193.5	2.26%	195.5	6.72%
Foreign banks due 2008	1.3	4.75%	3.4	5.83%
Bank loans due through 2012	10.8	6.02%	8.2	5.30%
Industrial development bonds due 2009	10.0	1.60%	10.0	3.77%
Capital lease obligations due through 2018	0.1	5.03%	0.4	4.89%
Other	—	—	0.6	7.79%
Subtotal	497.0	2.19%	514.4	6.34%
Less current portion and short-term debt	42.2	3.00%	28.6	6.03%
Total long-term debt, less current portion	<u>\$ 454.8</u>	<u>2.12%</u>	<u>\$ 485.8</u>	<u>6.36%</u>

On October 2, 2006, Armstrong executed a \$1.1 billion senior credit facility arranged by Banc of America Securities LLC, J.P. Morgan Securities, Inc., and Barclays Capital. This facility is made up of a \$300 million revolving credit facility (with a \$150 million sublimit for letters of credit), a \$300 million Term Loan A, and a \$500 million Term Loan B. This \$1.1 billion senior credit facility is secured by U.S. personal property (excluding land and buildings), the capital stock of material U.S. subsidiaries, and a 65% pledge of the stock of our material foreign subsidiaries.

The senior credit facility includes three financial covenants which do not permit the ratio of consolidated EBITDA to consolidated interest expense to be less than 3.00 to 1.00, the ratio of consolidated funded indebtedness to consolidated EBITDA (earnings before interest, taxes, depreciation and amortization) ("Consolidated Leverage Ratio") to be greater than 3.75 to 1.00 and that there is a minimum domestic liquidity of \$100 million, as defined by the credit agreement (incorporated in this 10-K as Exhibit 10.10). We are in compliance with these covenants. As of December 31, 2008 our consolidated interest coverage ratio was 12.98 to 1.00, our indebtedness to EBITDA was 1.24 to 1.00 and our domestic liquidity was \$452.9 million. We believe that the likelihood of default under these covenants is unlikely. Fully borrowing under our revolving credit facility, provided we maintain minimum domestic liquidity of \$100 million, would not violate these covenants.

The Revolving Credit and Term Loan A portions are currently priced at a spread of 1.50% over LIBOR and the Term Loan B portion is priced at 1.75% over LIBOR for its entire term. The Term Loan A and Term Loan B were both fully drawn down (net of scheduled and voluntary principal payments) and are currently priced on a variable interest rate basis. The unpaid balances of Term Loan A (\$281.3 million) and Term Loan B (\$193.5 million) of the credit facility may be prepaid without penalty at the maturity of their respective interest reset periods. Any amounts prepaid may not be reborrowed.

Prepayments of the loans under the senior credit facility are required unless (a) the Consolidated leverage ratio is less than or equal to 2.5:1.0, and (b) debt ratings from S&P is BB (stable) or better and from Moody's is Ba2 (stable) or better. If required, the prepayment amount would be 50% of Consolidated Excess Cash Flow (as defined in the agreement). Mandatory prepayments have not occurred since the inception of the agreement. Our current debt rating from S&P is BB (stable) and from Moody's is Ba2 (stable).

Approximately \$2.2 million of the remaining \$22.2 million of debt as of December 31, 2008 was secured with buildings and other assets. The credit lines at our foreign subsidiaries are subject to immaterial annual commitment fees.

As of December 31, 2007, approximately \$4.1 million of the \$22.7 million of total debt outstanding was secured with buildings and other assets.

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## Scheduled payments of long-term debt:

2009	\$ 40.9
2010	32.3
2011	234.8
2012	3.5
2013	184.1
2014 and later	0.1

We utilize lines of credit and other commercial commitments in order to ensure that adequate funds are available to meet operating requirements. On December 31, 2008, we had a \$300 million revolving credit facility with a \$150 million sublimit for letters of credit, of which \$49.6 million was outstanding. There were no outstanding borrowings under the revolving credit facility. Availability under this facility totaled \$250.4 million as of December 31, 2008. As of December 31, 2008, our foreign subsidiaries had available lines of credit totaling \$32.3 million, of which \$2.8 million was used and \$4.9 million was only available for letters of credit and guarantees, leaving \$24.6 million of unused lines of credit available for foreign borrowings.

On December 31, 2008, we had outstanding letters of credit totaling \$60.0 million, of which \$49.6 million was issued under the revolving credit facility and \$10.4 was arranged with another bank. Letters of credit are issued to third party suppliers, insurance and financial institutions and typically can only be drawn upon in the event of AWI's failure to pay its obligations to the beneficiary.

NOTE 19. PENSION AND OTHER BENEFIT PROGRAMS

We have defined benefit pension plans and postretirement medical and insurance benefit plans covering eligible employees worldwide. We also have defined-contribution pension plans for eligible employees. Benefits from defined benefit pension plans, which cover most employees worldwide, are based primarily on an employee's compensation and years of service. We fund our pension plans when appropriate. The U.S. defined benefit pension plans were closed to new salaried and salaried production employees on January 1, 2005. We also froze benefits for certain non-production salaried employees effective February 28, 2006. We fund postretirement benefits on a pay-as-you-go basis, with the retiree paying a portion of the cost for health care benefits by means of deductibles and contributions.

UNITED STATES PLANS

The following tables summarize the balance sheet impact of the pension and postretirement benefit plans, as well as the related benefit obligations, assets, funded status and rate assumptions. The pension benefits disclosures include both the Retirement Income Plan (RIP) and the Retirement Benefit Equity Plan, which is a nonqualified, unfunded plan designed to provide pension benefits in excess of the limits defined under Sections 415 and 401(a)(17) of the Internal Revenue Code.

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We use a December 31 measurement date for our U.S. defined benefit plans.

U.S. defined-benefit pension plans	Successor Company	
	Year 2008	Year 2007
<b>Change in benefit obligation:</b>		
Benefit obligation as of beginning of period	\$ 1,712.6	\$ 1,705.4
Service cost	17.4	16.9
Interest cost	97.8	96.3
Plan amendments	3.4	—
Actuarial loss	36.2	8.7
Benefits paid	(111.7)	(114.7)
Benefit obligation as of end of period	<u>\$ 1,755.7</u>	<u>\$ 1,712.6</u>
<b>Change in plan assets:</b>		
Fair value of plan assets as of beginning of period	\$ 2,355.7	\$ 2,238.7
Actual return on plan assets – (loss) gain	(545.6)	228.5
Employer contribution	3.2	3.2
Benefits paid	(111.7)	(114.7)
Fair value of plan assets as of end of period	<u>\$ 1,701.6</u>	<u>\$ 2,355.7</u>
Funded status of the plans	\$ (54.1)	\$ 643.1

U.S. defined-benefit pension plans	Successor Company	
	Year 2008	Year 2007
<b>Weighted-average assumptions used to determine benefit obligations at end of period:</b>		
Discount rate	5.60%	5.85%
Rate of compensation increase	4.00%	4.00%
<b>Weighted-average assumptions used to determine net periodic benefit cost for the period:</b>		
Discount rate	5.85%	5.75%
Expected return on plan assets	8.00%	8.00%
Rate of compensation increase	4.00%	4.00%

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U.S. defined-benefit retiree health and life insurance plans	Successor Company	
	Year 2008	Year 2007
<b>Change in benefit obligation:</b>		
Benefit obligation as of beginning of period	\$ 337.0	\$ 390.6
Service cost	1.7	1.8
Interest cost	18.9	19.1
Plan participants' contributions	6.2	6.7
Actuarial loss (gain)	1.4	(50.3)
Benefits paid, gross	(32.6)	(33.3)
Medicare subsidy receipts	1.7	2.4
Benefit obligation as of end of period	<u>\$ 334.3</u>	<u>\$ 337.0</u>
<b>Change in plan assets:</b>		
Fair value of plan assets as of beginning of period	—	—
Employer contribution	\$ 24.7	\$ 24.2
Plan participants' contributions	6.2	6.7
Benefits paid, gross	(32.6)	(33.3)
Medicare subsidy receipts	1.7	2.4
Fair value of plan assets as of end of period	<u>\$ —</u>	<u>\$ —</u>
Funded status of the plans	<u>\$ (334.3)</u>	<u>\$ (337.0)</u>

U.S. defined-benefit retiree health and life insurance plans	Successor Company	
	Year 2008	Year 2007
Weighted-average discount rate used to determine benefit obligations at end of period	5.60%	5.85%
Weighted-average discount rate used to determine net periodic benefit cost for the period	5.85%	5.75%

#### Investment Policies

The RIP's primary investment objective is to increase the ratio of RIP assets to liabilities by maximizing the long-term return on investments while minimizing the likelihood of cash contributions over the next 5-10 years. This is to be achieved by (a) investing primarily in publicly-traded equities, (b) limiting return volatility by diversifying investments among additional asset classes with differing expected rates of return and return correlations, and (c) investing a portion of RIP assets in a bond portfolio whose duration is roughly equal to the duration of RIP liabilities. Derivatives may be used either to implement investment positions efficiently or to hedge risk but not to create investment leverage.

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Each asset class utilized by the RIP has a defined asset allocation target and allowable range. The table below shows the asset allocation target and the December 31, 2008 and 2007 position for each asset class:

Asset Class	Successor Company		
	Target Weight at December 31, 2008	Position at December 31,	
		2008	2007
Domestic equity	41%	30%	38%
International equity	22%	17%	24%
High yield bonds	5%	4%	4%
Long duration bonds	25%	40%	27%
Real estate	7%	7%	6%
Other fixed income	0%	2%	1%

The difference between the target and actual positions as of December 31, 2008 is due to poor performance of the equity investments, not an intentional shift in asset allocation. In light of current market conditions, we are reevaluating our target asset allocations.

#### Basis of Rate-of-Return Assumption

Long-term asset class return assumptions are determined based on input from investment professionals on the expected performance of the asset classes over 10 to 20 years. The forecasts were averaged to come up with consensus passive return forecasts for each asset class. An incremental component was added for the expected return from active management based both on the RIP's experience and on historical information obtained from the RIP's investment consultants. These forecast gross returns were reduced by estimated management fees and expenses, yielding a long-term return forecast of 8.00% per annum.

Amounts recognized in assets and liabilities at year end consist of :

	Pension Benefits		Retiree Health and Life Insurance Benefits	
	Successor Company		Successor Company	
	2008	2007	2008	2007
Prepaid pension costs	—	\$ 687.8	—	—
Accounts payable and accrued expenses	\$ (3.3)	(3.4)	\$ (31.7)	\$ (30.2)
Postretirement and postemployment benefit liabilities	—	—	(302.6)	(306.8)
Pension benefit liabilities	(50.8)	(41.3)	—	—
Net amount recognized	\$ (54.1)	\$ 643.1	\$ (334.3)	\$ (337.0)

Pre-tax amounts recognized in accumulated other comprehensive income at year end consist of :

	Pension Benefits		Retiree Health and Life Insurance Benefits	
	Successor Company		Successor Company	
	2008	2007	2008	2007
Net actuarial loss (gain)	\$ 627.2	\$ (129.8)	\$ (46.2)	\$ (50.5)
Prior service cost	3.1	—	—	—
Accumulated other comprehensive loss (income)	\$ 630.3	\$ (129.8)	\$ (46.2)	\$ (50.5)

No amounts in accumulated other comprehensive loss (income) are expected to be amortized into the pension credit in 2009. We expect to amortize \$1.3 million of previously unrecognized net actuarial gains into postretirement benefit cost in 2009.





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The accumulated benefit obligation for the U.S. defined benefit pension plans was \$1,734.2 million and \$1,690.9 million at December 31, 2008 and 2007, respectively.

U.S. pension plans with benefit obligations in excess of assets	Successor Company	
	2008	2007
Projected benefit obligation, December 31	\$ 1,755.7	\$ 44.7
Accumulated benefit obligation, December 31	1,734.2	43.5
Fair value of plan assets, December 31	1,701.6	—

The increase in U.S. pension plans with benefit obligation in excess of assets occurred primarily because the RIP, which was previously overfunded, was underfunded in relation to its benefit obligations at December 31, 2008.

The components of pension credit are as follows :

U.S. defined-benefit pension plans	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Service cost of benefits earned during the period	\$ 17.4	\$ 16.9	\$ 3.4	\$ 13.6
Interest cost on projected benefit obligation	97.8	96.3	24.3	69.4
Expected return on plan assets	(175.3)	(169.4)	(42.5)	(121.5)
Amortization of prior service cost	0.3	—	—	6.7
Amortization of net actuarial loss	—	—	—	1.3
Net periodic pension credit	<u>\$ (59.8)</u>	<u>\$ (56.2)</u>	<u>\$ (14.8)</u>	<u>\$ (30.5)</u>

We recorded separate charges of \$0.5 million in the three months ended December 31, 2006 and \$8.5 million in the nine months ended September 30, 2006 within restructuring expense for special termination benefits related to the closure of certain operations at a manufacturing plant in Lancaster, Pennsylvania. See Note 16 for further information.

The components of postretirement benefit costs are as follows :

U.S. defined-benefit retiree health and life insurance plans	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Service cost of benefits earned during the period	\$ 1.7	\$ 1.8	\$ 0.7	\$ 1.8
Interest cost on accumulated postretirement benefit obligation	18.9	19.1	5.4	14.9
Amortization of prior service benefit	—	—	—	(4.8)
Amortization of net actuarial (gain) loss	(1.5)	(0.9)	—	9.4
Net periodic postretirement benefit cost	<u>\$ 19.1</u>	<u>\$ 20.0</u>	<u>\$ 6.1</u>	<u>\$ 21.3</u>

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For measurement purposes, average rates of annual increase in the per capita cost of covered health care benefits of 9.5% for pre-65 retirees and 10.0% for post-65 retirees were assumed for 2009, decreasing 1% per year to an ultimate rate of 5%. Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

U.S. retiree health and life insurance benefit plans	One percentage point	
	Increase	Decrease
Effect on total of service and interest cost components	\$ 0.5	\$ (0.5)
Effect on postretirement benefit obligation	7.9	(7.7)

We expect to contribute \$3.3 million to our U.S. defined benefit pension plans and \$31.7 million to our U.S. postretirement benefit plans in 2009.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid over the next ten years for our U.S. plans:

	Pension Benefits	Retiree Health and Life Insurance Benefits, Gross	Retiree Health Medicare Subsidy Receipts
2009	\$ 116.4	\$ 34.5	\$ (2.8)
2010	117.6	35.7	(3.0)
2011	120.7	36.4	(3.2)
2012	120.1	35.8	(3.4)
2013	122.4	33.8	(3.7)
2014–2018	635.9	153.6	(20.7)

**NON-U.S. PLANS**

We have defined benefit pension plans covering employees in a number of foreign countries that utilize assumptions which are consistent with, but not identical to, those of the U.S. plans. The following tables summarize the balance sheet impact of foreign pension benefit plans, as well as the related benefit obligations, assets, funded status and rate assumptions.

Effective with our adoption of FAS 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans," on October 2, 2006, we use a December 31 measurement date for all of our non-U.S. defined benefit plans. Prior to our adoption of FAS 158, we used a December 31 measurement date for most of our non-U.S. defined benefit plans.

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Non-U.S. defined-benefit plans	Successor Company	
	Year 2008	Year 2007
<b>Change in benefit obligation:</b>		
Benefit obligation as of beginning of period	\$ 403.0	\$ 406.5
Service cost	5.6	6.9
Interest cost	21.3	19.2
Plan participants' contributions	2.1	2.2
Foreign currency translation adjustment	(50.2)	29.2
Actuarial gain	(28.1)	(38.0)
Benefits paid	(24.5)	(23.0)
Benefit obligation as of end of period	<u>\$ 329.2</u>	<u>\$ 403.0</u>
<b>Change in plan assets:</b>		
Fair value of plan assets as of beginning of period	\$ 246.0	\$ 229.9
Actual return on plan assets — (loss) gain	(39.8)	7.8
Employer contributions	18.9	17.8
Plan participants' contributions	2.1	2.2
Foreign currency translation adjustment	(46.6)	11.3
Benefits paid	(24.5)	(23.0)
Fair value of plan assets as of end of period	<u>\$ 156.1</u>	<u>\$ 246.0</u>
Funded status of the plans	\$ (173.1)	\$ (157.0)
<b>Weighted-average assumptions used to determine benefit obligations at end of period:</b>		
<b>Successor Company</b>		
Year 2008      Year 2007		
Discount rate	5.9%	5.5%
Rate of compensation increase	3.4%	3.5%
<b>Weighted-average assumptions used to determine net periodic benefit cost for the period:</b>		
Discount rate	5.5%	4.7%
Expected return on plan assets	6.7%	6.6%
Rate of compensation increase	3.5%	3.2%

#### Investment Policies

Each of the funded non-US pension plan's primary investment objective is to earn sufficient long-term returns on investments both to increase the ratio of the assets to liabilities in order for the plans to meet their benefits obligations, and to minimize required cash contributions to the plans. This is to be achieved by (a) investing primarily in publicly-traded equities, (b) limiting return volatility by diversifying investments among additional asset classes with differing expected rates of return and return correlations, and (c) utilizing long duration bonds to limit the volatility of the plans' asset/liability ratios.

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Each of the plans has a targeted asset allocation for each asset class. The table below shows, for each asset class, the weighted average of the several plans' asset allocation targets and positions at December 31, 2008 and 2007:

Asset Class	Successor Company		
	Target Weight at December 31, 2008	Position at December 31, 2008	2007
Equities	58%	56%	61%
Long duration bonds	24%	26%	23%
Other fixed income	10%	12%	10%
Real estate	8%	6%	6%

Basis of Rate-of-Return Assumption

Long-term asset class return forecasts were obtained from investment professionals. The forecasts were averaged to come up with consensus passive return forecasts for each asset class. These forecast asset class returns were weighted by the plans' target asset class weights, yielding a long-term return forecast of 6.7% for the year ended December 31, 2008 and 6.6% for the year ended December 31, 2007.

Amounts recognized in the consolidated balance sheets consist of:

	Successor Company	
	2008	2007
Prepaid pension costs	\$ 0.3	\$ 20.2
Accounts payable and accrued expenses	(12.8)	(13.0)
Pension benefit liabilities	(160.6)	(164.2)
Net amount recognized	<u>\$ (173.1)</u>	<u>\$ (157.0)</u>

Pre-tax amounts recognized in accumulated other comprehensive income at year end consist of:

	Successor Company	
	2008	2007
Net actuarial (gain)	\$ (14.1)	\$ (41.7)
Prior service cost (credit)	—	—
Accumulated other comprehensive (income)	<u>\$ (14.1)</u>	<u>\$ (41.7)</u>

We expect to amortize \$0.5 million of previously unrecognized net actuarial losses into pension cost in 2009.

The accumulated benefit obligation for the non-U.S. defined benefit pension plans was \$309.0 million and \$376.0 million at December 31, 2008 and 2007, respectively.

Non-U.S. pension plans with benefit obligations in excess of assets	Successor Company	
	2008	2007
Projected benefit obligation, December 31	\$ 328.3	\$ 177.2
Accrued benefit obligation, December 31	308.1	172.0
Fair value of plan assets, December 31	154.9	—

The increase in non-U.S. pension plans with benefit obligation in excess of assets occurred primarily because three of our previously overfunded plans were underfunded in relation to their benefit obligations at December 31, 2008.

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The components of pension cost are as follows:

	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Non-U.S. defined-benefit plans				
Service cost of benefits earned during the period	\$ 5.6	\$ 6.9	\$ 1.7	\$ 5.1
Interest cost on projected benefit obligation	21.3	19.2	4.5	12.3
Expected return on plan assets	(16.0)	(15.4)	(3.6)	(8.6)
Amortization of transition obligation (asset)	—	—	—	(0.1)
Amortization of prior service cost	—	—	—	0.4
Amortization of net actuarial gain	(0.5)	—	—	2.1
Net periodic pension cost	<u>\$ 10.4</u>	<u>\$ 10.7</u>	<u>\$ 2.6</u>	<u>\$ 11.2</u>

We expect to contribute \$18.3 million to our non-U.S. defined benefit pension plans in 2009.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid over the next ten years:

	Pension Benefits
2009	\$ 21.1
2010	20.9
2011	21.9
2012	20.8
2013	22.7
2014–2018	119.8

Costs for other worldwide defined contribution benefit plans and multiemployer pension plans were \$14.8 million in 2008, \$15.2 million in 2007, \$3.3 million in the three months ended December 31, 2006 and \$9.6 million in the nine months ended September 30, 2006.

#### NOTE 20. FINANCIAL INSTRUMENTS

We do not hold or issue financial instruments for trading purposes. The estimated fair values of our financial instruments are as follows:

(millions at December 31)	Successor Company			
	2008		2007	
	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Assets/(Liabilities):				
Long-term debt, including current portion	\$ (495.7)	\$ (405.0)	\$ (510.5)	\$ (502.0)
Foreign currency contract obligations	7.4	7.4	(5.0)	(5.0)
Natural gas contracts	(13.5)	(13.5)	(1.5)	(1.5)

The carrying amounts of cash and cash equivalents, receivables, accounts payable and accrued expenses, short-term debt and current installments of long-term debt approximate fair value because of the short-term maturity of these instruments. The fair value estimates of long-term debt were based upon quotes from major financial institutions taking into consideration current rates offered to us for debt of the same remaining maturities. The fair value estimates of foreign currency contract obligations are



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estimated from national exchange quotes. The fair value estimates of natural gas contracts are estimated by obtaining quotes from major financial institutions.

As discussed in Note 2, we adopted FAS 157 effective January 1, 2008, with respect to the fair value measurement and disclosure of financial assets and liabilities. FAS 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. FAS 157 establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities.

Level 2 — Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

	Successor Company			
	2008		2007	
	Fair value based on			
(millions at December 31)	Quoted, active markets "Level 1"	Other observable inputs "Level 2"	Quoted, active markets "Level 1"	Other observable inputs "Level 2"
<b>Assets/(Liabilities):</b>				
Foreign currency contract obligations	\$ 7.4	—	\$ (5.0)	—
Natural gas contracts	—	\$ (13.5)	—	\$ (1.5)

We do not have any financial derivative assets or liabilities that are valued using Level 3 (unobservable) inputs.

#### NOTE 21. DERIVATIVE FINANCIAL INSTRUMENTS

We are exposed to market risk from changes in foreign currency exchange rates, interest rates and commodity prices that could impact our results of operations and financial condition. We use forward swaps and option contracts to hedge currency and commodity exposures. We regularly monitor developments in the capital markets and only enter into currency and swap transactions with established counterparties having investment grade ratings. Exposure to individual counterparties is controlled and derivative financial instruments are entered into with a diversified group of major financial institutions. Forward swaps and option contracts are entered into for periods consistent with underlying exposure and do not constitute positions independent of those exposures. At inception, we formally designate and document our derivatives as either (1) a hedge of a forecasted transaction or "cash flow" hedge, or (2) a hedge of the fair value of a recognized liability or asset or "fair value" hedge. We also formally assess, both at inception and at least quarterly thereafter, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in either the fair value or cash flows of the hedged item. If it is determined that a derivative ceases to be a highly effective hedge, or if the anticipated



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transaction is no longer likely to occur, we discontinue hedge accounting, and any deferred gains or losses are recognized in earnings. We use derivative financial instruments as risk management tools and not for speculative trading purposes.

Interest Rate Risk — There were no open interest rate derivatives as of December 31, 2008 and 2007. In February 2009 we entered into interest rate swaps with a total notional amount of \$100 million that mature in December 2009. Under the terms of the swaps, we receive 1-month LIBOR and pay a fixed rate over the hedged period. These swaps are designated as cash flow hedges to hedge against changes in LIBOR for a portion of our variable rate debt.

Currency Rate Risk — We manufacture and sell our products in a number of countries throughout the world and, as a result, are exposed to movements in foreign currency exchange rates. To a large extent, our global manufacturing and sales provide a natural hedge of foreign currency exchange rate movement, as foreign currency expenses generally offset foreign currency revenues. We manage our cash flow exposures on a net basis and use derivatives to hedge our unmatched foreign currency cash inflows and outflows. At December 31, 2008, our major foreign currency exposures are to the Euro, the Canadian dollar, and the British pound.

We use foreign currency forward exchange contracts to reduce our exposure to the risk that the eventual net cash inflows and outflows, resulting from the sale of product to foreign customers and purchases from foreign suppliers, will be adversely affected by changes in exchange rates. These derivative instruments are used for forecasted transactions and are classified as cash flow hedges. Cash flow hedges are executed quarterly for up to 15 months forward and allow us to further reduce our overall exposure to exchange rate movements, since the gains and losses on these contracts offset losses and gains on the transactions being hedged. Gains and losses on these instruments are deferred in other comprehensive income until the underlying transaction is recognized in earnings. The net fair value of these instruments at December 31, 2008 was an asset of \$6.4 million. A gain of \$6.4 million is included in other comprehensive income related to changes in the fair value of our foreign currency forward exchange contracts, \$6.3 million of which is expected to be recorded to earnings in the next twelve months. The earnings impact is reported in either net sales or cost of goods sold to match the underlying transaction being hedged. The earnings impact of these type of hedges was a total gain of less than \$0.3 million recorded during 2008. The earnings impact of the ineffective portion of these hedges was not material during 2008. There were no circumstances where hedge treatment was discontinued during 2008.

We also use foreign currency forward exchange contracts to hedge exposures created by cross-currency intercompany loans. The underlying intercompany loans are classified as short-term and translation adjustments related to these loans are recorded in other non-operating income or expense. The offsetting gains and losses on the related derivative contracts are also recorded in other non-operating income or expense. These transactions are generally executed on a six-month rolling basis and are offset or increased as repayment or additional intercompany loans are extended. The fair value of these instruments at December 31, 2008 was an asset of \$1.0 million. During 2008, the net earnings impact of these transactions was a gain of \$0.3 million recorded in other non-operating income.

Our foreign currency hedges are typically 'forward sale' or 'forward buy' contracts whose prices are actively traded and that are readily identifiable in the global currency markets. The current market values of forward currency positions are highly calculable (quotable) at any point in time by pegging the current, observable, spot rate for the currency to an ultimate contract maturity date. Consequently, the pricing we use to measure our foreign exchange hedges are based on observable inputs and are thus "Level 1" pricing inputs as defined in the FAS 157 hierarchy.

Commodity Price Risk — We purchase natural gas for use in the manufacture of ceiling tiles and other products and to heat many of our facilities. As a result, we are exposed to movements in the price of natural gas. We have a policy of reducing cost volatility for North American natural gas purchases by purchasing natural gas forward contracts, purchased call options, and zero-cost collars up to 15 months forward to reduce our overall exposure to natural gas price movements. There is a high correlation

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between the hedged item and the hedged instrument. The gains and losses on these transactions offset losses and gains on the transactions being hedged. These instruments are designated as cash flow hedges. The mark-to-market gain or loss on qualifying hedges is included in other comprehensive income to the extent effective, and reclassified into cost of goods sold in the period during which the underlying products are sold. The mark-to-market gains or losses on ineffective portions of hedges are recognized in cost of goods sold immediately. There were no circumstances where hedge treatment was discontinued during 2008. The fair value of these instruments at December 31, 2008 was a \$13.5 million liability. There is also a loss of \$13.2 million included in other comprehensive income related to changes in the fair value of our natural gas hedge contracts, of which \$12.0 million is expected to be recorded to earnings in the next twelve months. A loss of \$1.2 million is expected to be recorded to earnings in 2010. The earnings impact of hedges that matured during 2008, recorded in cost of goods sold, was \$1.2 million of income. The earnings impact of the ineffective portion of these hedges was not material during 2008.

Our natural gas contracts derive their basis in the NYMEX or other commodity exchanges, but are transacted 'over-the-counter' and tailored to suit the specific trade parameters (i.e.: maturity, size, underlying Btu's) required by our North American operations. Thus, instead of having precisely observable inputs, the pricing is based upon similar, generic pricing of other market-traded contracts.

We use two sources to derive the fair value of our natural gas hedges. First, each of our counterparties provides us with indicative fair values as calculated from their own proprietary models. Second, we have developed our own methodology to derive a fair value for our natural gas hedges based on the Black-Scholes option valuation model. We obtain market information including current time to maturity, risk free rates, implied volatility and the current forward price. We have compared our own derived fair values with those provided by our counterparties and have noted the differences are immaterial. Accordingly, we consider the fair values used for our Natural Gas hedges to be fairly stated and the pricing inputs used for those fair values to be within the "Level 2" category of the FAS 157 hierarchy.

There have been no changes to the valuation techniques used during the periods presented.

NOTE 22. GUARANTEES

In disposing of assets, AWI and some subsidiaries have entered into contracts that included various indemnity provisions, covering such matters as taxes, environmental liabilities and asbestos and other litigation. Some of these contracts have exposure limits, but many do not. Due to the nature of the indemnities, it is not possible to estimate the potential maximum exposure under these contracts. For contracts under which an indemnity claim has been received, a liability of \$5.8 million has been recorded as of December 31, 2008. See Note 32 of the Consolidated Financial Statements for additional information.

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**NOTE 23. PRODUCT WARRANTIES**

We provide direct customer and end-user warranties for our products. These warranties cover manufacturing defects that would prevent the product from performing in line with its intended and marketed use. The terms of these warranties vary by product and generally provide for the repair or replacement of the defective product. We collect and analyze warranty claims data with a focus on the historic amount of claims, the products involved, the amount of time between the warranty claims and their respective sales and the amount of current sales. The following table summarizes the activity for the accrual of product warranties for 2008 and 2007:

	Successor Company	
	Year 2008	Year 2007
Balance at beginning of period	\$ 17.6	\$ 21.2
Reductions for payments	(24.9)	(24.5)
Current period warranty accruals	25.1	21.4
Preexisting warranty accrual changes	(1.2)	(0.9)
Effects of foreign exchange translation	(0.3)	0.4
Balance at end of period	<u>\$ 16.3</u>	<u>\$ 17.6</u>

The warranty reserve is recorded as a reduction of sales and accounts receivable.

**NOTE 24. OTHER LONG-TERM LIABILITIES**

	Successor Company	
	December 31, 2008	December 31, 2007
Long-term deferred compensation arrangements	\$ 30.4	\$ 35.7
U.S. workers' compensation	13.4	15.8
Environmental liabilities	6.5	7.0
Other	12.1	9.3
Total other long-term liabilities	<u>\$ 62.4</u>	<u>\$ 67.8</u>

**NOTE 25. STOCK-BASED COMPENSATION PLANS**

Predecessor Company

Awards under the Predecessor Company's stock-based compensation plans were made in the form of stock options, stock appreciation rights in conjunction with stock options, performance restricted shares, stock awards and restricted stock awards. All of the Predecessor Company plans were terminated upon AWI emerging from Chapter 11 on October 2, 2006.

Options were granted to purchase shares at prices not less than the closing market price of the shares on the dates the options were granted. The options generally became exercisable in one to three years and expired 10 years from the date of grant.

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	<u>Predecessor Company</u> Nine Months Ended September 30, 2006
Changes in AHI option shares outstanding (thousands except for share price)	
Option shares at beginning of period	1,987.3
Options granted	—
Option shares exercised	—
Options forfeited	(23.8)
Options expired	(189.8)
Option shares at end of period	1,773.7
Option shares exercisable at end of period	1,773.7
Shares available for grant	5,029.0
Weighted average price per share:	
Options outstanding	\$ 24.67
Options exercisable	\$ 24.67

Although the plans under which these options were issued were terminated upon AWI's emerging from Chapter 11, the existing option contracts remained enforceable against AHI until AHI's liquidation in December 2007. Reorganized Armstrong has no further liability under these plans.

Restricted stock awards were used for the purposes of recruitment, special recognition and retention of key employees. As of September 30, 2006, no award of restricted stock shares had been granted since 2000. As of September 30, 2006, there were 111,463 restricted shares of AHI common stock outstanding with 596 accumulated dividend equivalent shares. These awards expired upon AWI's emerging from Chapter 11 on October 2, 2006.

#### Successor Company

As of October 2, 2006, the Board of Directors of reorganized AWI adopted and the then sole shareholder of AWI approved, reorganized Armstrong's 2006 Long-Term Incentive Plan ("2006 Plan").

The 2006 Plan authorizes us to issue stock options, stock appreciation rights, restricted stock awards, stock units, performance-based awards and cash awards to officers and key employees. No more than 5,349,000 common shares may be issued under the 2006 Plan, and the 2006 Plan will terminate on October 2, 2016, after which time no further awards may be made. As of December 31, 2008, 3,092,888 shares were available for future grants under the 2006 plan.

For grants made between our Chapter 11 emergence on October 2, 2006 and October 17, 2006, options were granted to purchase shares at a price equal to the volume weighted average closing price of the shares for the period October 18, 2006 through October 31, 2006. For grants made on or after October 18, 2006, options were granted to purchase shares at prices equal to the closing market price of the shares on the dates the options were granted. The options generally become exercisable in two to four years and expire 10 years from the date of grant.

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	Successor Company Year Ended December 31, 2008			
	Number of shares (thousands)	Weighted- average exercise price	Weighted- average remaining contractual term (years)	Aggregate intrinsic value (millions)
Option shares outstanding at beginning of period	1,569.8	\$ 38.99		
Options granted	195.7	29.73		
Option adjustment for March dividend (see below)	95.8	29.16		
Option shares exercised	—	—		
Options forfeited	(328.4)	(31.02)		
Option shares outstanding at end of period	1,532.9	\$ 29.85	7.9	—
Option shares exercisable at end of period	505.8	29.85	7.9	—
Option shares expected to vest	936.6	30.17		—

	Successor Company Year Ended December 31, 2007			
	Number of shares (thousands)	Weighted- average exercise price	Weighted- average remaining contractual term (years)	Aggregate intrinsic value (millions)
Option shares outstanding at beginning of period	1,592.0	\$ 38.42		
Options granted	64.1	52.38		
Option shares exercised	—	—		
Options forfeited	(86.3)	(38.47)		
Option shares outstanding at end of period	1,569.8	\$ 38.99	8.8	\$ 2.5
Option shares exercisable at end of period	—	—	—	—
Option shares expected to vest	1,516.4	—	—	\$ 2.5

We have reserved sufficient authorized shares to allow us to issue new shares upon exercise of all outstanding options. When options are actually exercised, we will issue new shares, use treasury shares (if available), acquire shares held by investors, or a combination of these alternatives in order to satisfy the option exercises.

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The fair value of option grants was estimated on the date of grant using the Black-Scholes option pricing model. The weighted average assumptions for the years 2008 and 2007 and the three months ended December 31, 2006 are presented in the table below.

	Successor Company		
	Year 2008	Year 2007	Three Months Ended December 31, 2006
Weighted-average grant date fair value of options granted (dollars per option)	\$ 12.21	\$ 20.64	\$ 15.51
Assumptions			
Risk free rate of return	3.2%	4.8%	4.6%
Expected volatility	29.8%	30.2%	33.2%
Expected term (in years)	6.0	6.0	6.5
Expected dividend yield	0.0%	0.0%	0.0%

The risk free rate of return is determined based on the implied yield available on zero coupon U.S. Treasury bills at the time of grant with a remaining term equal to the expected term of the option. Because reorganized Armstrong's stock has been trading for only a short period of time, the expected volatility is established based on an average of the actual historical volatilities of the stock prices of a peer group of companies. The expected life is the midpoint of the average vesting period and the contractual life of the grant. For the same reasons mentioned earlier we are using an allowable simplified method to determine an appropriate expected term for our option valuation assumptions. The expected dividend yield is assumed to be zero because, at the time of each grant, we had no plans to declare a dividend. The assumptions outlined above are applicable to all option grants.

Under the terms of the 2006 Long Term Incentive Plan ("the Plan"), the Management Development and Compensation Committee ("the Committee") of our Board of Directors is required to make equitable adjustments to stock option grants if there is a change in our capital structure. The special cash dividend qualified as a change to our capital structure under the terms of the Plan. We used the Black-Scholes option pricing model to determine the fair value of the awards before and after the special cash dividend, using consistent assumptions for the risk free rate of return, expected term, expected volatility and expected dividend yield. The stock prices used in the before and after calculations were \$35.10 (the closing price on March 6, 2008, the day before the ex-dividend date) and \$29.37 (the closing price on March 7, 2008, the ex-dividend date), respectively. For all option grants, the fair value of the award before and after the dividend remained the same. Therefore, in accordance with Statement of Financial Accounting Standards No. 123R, "Share-Based Payment", there was no incremental cost recognized in our financial statements due to these award modifications. The following changes were made to the options outstanding as a result of this change:

	Original Grant Terms		Adjusted Grant Terms	
	Number of Shares	Exercise Price	Number of Shares	Exercise Price
Options granted in 2006	1,445,700	\$ 38.42	1,520,024	\$ 29.37
Options granted in 2007	64,100	52.38	64,100	39.88
Options granted in 2008	110,370	34.00	131,904	28.45

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In addition to options, we also granted restricted stock and restricted stock units. These awards generally have vesting periods of two to four years. A summary of these awards follows:

	Successor Company Non-Vested Stock Awards	
	Number of Shares	Weighted- average fair value at grant date
January 1, 2007	530,650	\$ 36.96
Granted	91,559	52.38
Vested	—	—
Forfeited	(31,275)	(39.12)
December 31, 2007	590,934	\$ 39.24
Granted	307,866	32.61
Vested	(152,945)	36.89
Forfeited	(138,369)	37.54
December 31, 2008	607,486	\$ 36.86

In 2008 and 2007, we granted 58,390 and 37,900 performance restricted shares, respectively, to the company CEO, which entitles him to receive a specified number of shares of reorganized Armstrong's common stock on various vesting dates, provided certain cumulative financial targets are achieved over the three-year performance period. We estimated the fair value of performance share awards based on the market price of the underlying stock on the date of grant.

In addition to the equity awards described above, as of December 31, 2007 we had granted 81,244 phantom shares under the 2006 Phantom Stock Unit Plan to non-employee directors which will be settled in the future for cash. During 2008, 50,320 of the phantom shares were converted to restricted stock units leaving a balance of 30,924 phantom shares outstanding at December 31, 2008. These awards generally have vesting periods of one to three years, and as of December 31, 2008, 24,924 shares were vested. The awards are generally payable six months following the director's separation from service. The total liability recorded for these shares as of December 31, 2008 was \$0.9 million.

During 2008, we adopted the 2008 Directors Stock Unit Plan. The 2006 Phantom Stock Unit Plan is still in place; however, no additional shares will be granted under that plan. Under the 2008 Directors Stock Unit Plan we currently have 111,950 restricted stock units outstanding. In 2008, we granted 61,630 restricted stock units to non-employee directors and as noted above 50,320 shares were converted from phantom shares. These awards generally have vesting periods of one to three years, and as of December 31, 2008, 38,320 shares were vested. The awards are generally payable six months following the director's separation from service. The awards under the stock unit plans are not reflected in the Non-Vested Stock Awards table above.

We recognize compensation expense on a straight-line basis over the vesting period. Share-based compensation cost was \$8.1 million (\$5.2 million net of tax benefit) in 2008, \$13.6 million (\$9.1 million net of tax benefit) in 2007 and \$2.5 million (\$1.5 million net of tax benefit) in the three months ended December 31, 2006. The decrease in share-based compensation cost from 2007 to 2008 is the result of an increase in forfeitures in 2008. Share-based compensation expense is recorded as a component of SG&A expenses. There has been no cash flow impact to date of these awards.

As of December 31, 2008, there was \$24.4 million of total unrecognized compensation cost related to non-vested share-based compensation arrangements. That cost is expected to be recognized over a weighted-average period of 2.1 years.

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**NOTE 26. EMPLOYEE COMPENSATION**

Employee compensation is presented in the table below. Charges for severance costs and early retirement incentives to terminated employees that were otherwise recorded as restructuring charges have been excluded.

	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Employee compensation cost				
Wages, salaries and incentive compensation	\$ 718.1	\$ 755.8	\$ 180.0	\$ 555.6
Payroll taxes	75.6	77.1	16.9	55.3
Pension expense (credits), net	(34.6)	(30.3)	(8.9)	(9.7)
Insurance and other benefit costs	77.5	84.0	23.3	64.2
Stock-based compensation	8.1	13.6	2.5	—
Total	<u>\$ 844.7</u>	<u>\$ 900.2</u>	<u>\$ 213.8</u>	<u>\$ 665.4</u>

**NOTE 27. LEASES**

We rent certain real estate and equipment. Several leases include options for renewal or purchase, and contain clauses for payment of real estate taxes and insurance. In most cases, management expects that in the normal course of business, leases will be renewed or replaced by other leases.

Rental expense was \$22.8 million in the year 2008, \$22.7 million in the year 2007, \$5.5 million in the three months ended December 31, 2006 and \$15.9 million in the nine months ended September 30, 2006. Future minimum payments at December 31, 2008, by year and in the aggregate, having noncancelable lease terms in excess of one year were as follows:

Scheduled minimum lease payments	Operating Leases
2009	\$ 14.9
2010	10.6
2011	6.7
2012	3.5
2013	2.1
Thereafter	4.7
Total	<u>\$ 42.5</u>



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NOTE 28. SHAREHOLDERS' EQUITY

There were no Successor Company treasury shares at December 31, 2008 or December 31, 2007.

The balance of each component of accumulated other comprehensive (loss) income as of December 31, 2008 and 2007 is presented in the table below.

	Successor Company	
	December 31, 2008	December 31, 2007
Foreign currency translation adjustments	\$ (9.4)	\$ 32.7
Derivative (loss), net	(3.3)	(4.7)
Pension and postretirement adjustments	(335.0)	148.5
Accumulated other comprehensive (loss) income	<u>\$ (347.7)</u>	<u>\$ 176.5</u>

The amounts and related tax effects allocated to each component of other comprehensive (loss) income during 2008 are presented in the table below.

	Successor Company		
	Pre-tax Amount	Tax Benefit	After tax Amount
Foreign currency translation adjustments	\$ (49.2)	\$ 7.1	\$ (42.1)
Derivative gain (loss), net	0.7	0.7	1.4
Pension and postretirement adjustments	(792.0)	308.5	(483.5)
Total other comprehensive (loss) income	<u>\$ (840.5)</u>	<u>\$ 316.3</u>	<u>\$ (524.2)</u>

NOTE 29. SUPPLEMENTAL FINANCIAL INFORMATION

	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
<b>Selected operating expenses</b>				
Maintenance and repair costs	\$ 111.3	\$ 116.9	\$ 27.6	\$ 88.3
Research and development costs	38.8	44.0	11.5	32.4
Advertising costs	29.6	36.2	6.1	22.7
<b>Other non-operating expense</b>				
Foreign currency translation loss, net of hedging activity	\$ 1.1	\$ 0.7	—	—
Other	0.2	0.7	\$ 0.3	\$ 1.0
<b>Total</b>	<u>\$ 1.3</u>	<u>\$ 1.4</u>	<u>\$ 0.3</u>	<u>\$ 1.0</u>
<b>Other non-operating income</b>				
Interest income	\$ 10.5	\$ 15.3	\$ 4.0	\$ 2.9
Foreign currency translation gain, net of hedging activity	0.1	2.5	0.3	4.2
Other	—	0.4	—	0.1
<b>Total</b>	<u>\$ 10.6</u>	<u>\$ 18.2</u>	<u>\$ 4.3</u>	<u>\$ 7.2</u>



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NOTE 30. SUPPLEMENTAL CASH FLOW INFORMATION

	Successor Company			Predecessor Company
	Year 2008	Year 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
Interest paid	\$ 23.7	\$ 47.8	\$ 9.9	\$ 0.7
Income taxes (refunded) paid, net	25.7	(181.4)	7.5	56.6

NOTE 31. RELATED PARTIES

We purchase grid products from WAVE, our 50%-owned joint venture with Worthington Industries. The total amount of these purchases was approximately \$98 million in the year 2008, \$88 million in the year 2007, \$22 million in the three months ended December 31, 2006 and \$54 million in the nine months ended September 30, 2006. We also provide certain selling, promotional and administrative processing services to WAVE for which we receive reimbursement. Those services amounted to \$16.1 million in the year 2008, \$15.0 million in the year 2007, \$3.4 million in the three months ended December 31, 2006 and \$10.3 million in the nine months ended September 30, 2006. The net amounts due from us to WAVE for all of our relationships were \$2.8 million and \$5.8 million at the end of 2008 and 2007, respectively. See Note 11 for additional information.

NOTE 32. LITIGATION AND RELATED MATTERSASBESTOS-RELATED LITIGATION

On October 2, 2006 AWI's plan of reorganization, which was confirmed by order dated August 18, 2006, became effective, and AWI emerged from Chapter 11. The following summarizes how the asbestos-related litigation matters were impacted by AWI's emergence. See Note 1 for additional information.

Prior to December 6, 2000, AWI had been named as a defendant in personal injury cases and property damage cases related to asbestos-containing products. On December 6, 2000, AWI filed a voluntary petition for relief ("the Filing") under Chapter 11 of the U.S. Bankruptcy Code to use the court-supervised reorganization process to achieve a resolution of AWI's asbestos-related liability.

Two of AWI's domestic subsidiaries also commenced Chapter 11 proceedings at the time of the Filing. AWI's other direct and indirect subsidiaries and affiliates, including Armstrong Wood Products Inc. (formerly Triangle Pacific Corp.), WAVE (Armstrong's ceiling grid systems joint venture with Worthington Industries, Inc.), Armstrong Canada and Armstrong DLW AG were not a part of the Filing and accordingly the liabilities, including asbestos-related liability if any, of such companies arising out of their own activities were not resolved in AWI's Chapter 11 Case except for any asbestos-related liability that also relates, directly or indirectly, to the pre-Filing activities of AWI.

Upon AWI's POR becoming effective on October 2, 2006, the Asbestos PI Trust was created for the purpose of addressing and resolving AWI's personal injury (including wrongful death) asbestos-related liability. As of October 2, 2006, all present and future asbestos-related personal injury claims against AWI, including contribution claims of co-defendants, arising directly or indirectly out of AWI's pre-Filing use of or other activities involving asbestos, were channeled to the Asbestos PI Trust.

As part of the POR, in accordance with an injunction issued under Section 524(g) of the Bankruptcy Code and entered in connection with the POR, various entities are protected from present and future asbestos-related personal injury claims. These entities include, among others, reorganized Armstrong, AHI, AWI's subsidiaries and other affiliates (as defined in the POR), and their respective officers and directors. Now that it has emerged from Chapter 11, AWI does not have any responsibility for these claims (including claims against AWI based solely on its ownership of a subsidiary or other affiliate), nor does it participate



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in their resolution. Accordingly, AWI has no recorded liability for asbestos-related personal injury claims as of December 31, 2008 and December 31, 2007.

On October 2, 2006, pursuant to the POR becoming effective, AWI transferred to the Asbestos PI Trust rights arising under liability insurance policies issued to AWI with respect to asbestos-related personal injury claims. As of October 2, 2006, resolution of asbestos-related personal injury insurance matters is the responsibility of the Asbestos PI Trust. As part of accounting for emergence, AWI reflected the transfer of these rights to the Asbestos PI Trust. Therefore, there is no recorded insurance asset in respect of asbestos claims as of December 31, 2008 and December 31, 2007.

Asbestos-related personal injury claims against the affiliates and subsidiaries of AWI covered by the POR will be channeled to the Asbestos PI Trust only to the extent such claims directly or indirectly relate to the manufacturing, installation, distribution or other activities of AWI or are based solely on AWI's ownership of the subsidiaries or other affiliates (as distinguished from independent activities of the subsidiaries or affiliates). Currently, one asbestos-related personal injury lawsuit against a subsidiary of AWI allegedly arising out of such independent activities is pending. This claim will not be channeled to the Asbestos PI Trust under the POR. The subsidiary denies liability and is aggressively defending the matter. AWI has not recorded any liability for this matter. Management does not expect that any sum that may be paid in connection with this matter will be material to reorganized Armstrong.

In addition, workers' compensation claims brought against AWI or its subsidiaries or other affiliates will not be channeled to the Asbestos PI Trust. These claims remain subject to the workers' compensation process. Historically, workers' compensation claims against AWI and its subsidiaries have not been significant in number or amount. AWI honored its obligations with respect to such claims during the Chapter 11 Case and following emergence. Workers' compensation law provides that the employer is responsible for evaluation, medical treatment and lost wages as a result of a job-related injury. Currently, AWI has nine pending workers' compensation claims, and a UK subsidiary has eleven employer liability claims involving alleged asbestos exposure.

There is uncertainty as to the effectiveness of the 524(g) injunction in precluding the assertion in foreign jurisdictions of asbestos-related personal injury claims, proceedings related thereto or the enforcement of judgments rendered in such proceedings.

Management believes that AWI, its subsidiaries and other affiliates are not subject to any asbestos-related personal injury claims that will not be channeled to the Asbestos PI Trust under the POR that, individually or collectively, would be material in amount to reorganized Armstrong.

## ENVIRONMENTAL MATTERS

### Environmental Expenditures

Our manufacturing and research facilities are affected by various federal, state and local requirements relating to the discharge of materials and the protection of the environment. We make expenditures necessary for compliance with applicable environmental requirements at each of our operating facilities. Regulatory requirements continually change, therefore we cannot predict with certainty future expenditures associated with compliance with environmental requirements.

### Environmental Remediation

#### *Summary*

We are actively involved in proceedings under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), and similar state "Superfund" laws at four off-site locations. We have also been investigating and/or remediating environmental contamination allegedly resulting from past industrial activity at five domestic and five foreign current or former plant sites. In most cases, we are one of many potentially responsible parties ("PRPs") which have potential liability for the required investigation and remediation of each site. In some cases, we have agreed to jointly fund that required investigation and remediation, while at some sites, we dispute the liability, the proposed remedy or the



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proposed cost allocation among the PRPs. We may also have rights of contribution or reimbursement from other parties or coverage under applicable insurance policies.

Estimates of our future environmental liability at the Superfund sites and current or former plant sites are based on evaluations of currently available facts regarding each individual site and consider factors such as our activities in conjunction with the site, existing technology, presently enacted laws and regulations and prior company experience in remediating contaminated sites. Although current law imposes joint and several liability on all parties at Superfund sites, our contribution to the remediation of these sites is expected to be limited by the number of other companies potentially liable for site remediation. As a result, our estimated liability reflects only our expected share. In determining the probability of contribution, we consider the solvency of other parties, whether liability is being disputed, the terms of any existing agreements and experience with similar matters, and the impact of AWI's emergence from Chapter 11 upon the validity of the claim.

*Effects of Chapter 11*

Upon AWI's emergence from Chapter 11 on October 2, 2006, AWI's environmental liabilities with respect to properties that AWI does not own or operate (such as formerly owned sites, or landfills to which AWI's waste was taken) were discharged. Claims brought by a federal or state agency alleging that AWI should reimburse the claimant for money that it spent cleaning up a site which AWI does not own or operate, and claims by private parties, such as other PRPs with respect to sites with multiple PRPs, were discharged upon emergence. Now that it has emerged from Chapter 11, AWI does not have any responsibility for these claims. Environmental obligations with respect to AWI's subsidiaries and to property that they currently own or operate have not been discharged.

In addition to the right to sue for reimbursement of the money it spends, however, CERCLA also gives the federal government the right to sue for an injunction compelling a defendant to perform a cleanup. Several state statutes give similar injunctive rights to those states. While we believe such rights against AWI were also discharged upon AWI's emergence from Chapter 11, there does not appear to be controlling judicial precedent in that regard. Thus, according to some cases, while a governmental agency's right to require AWI to reimburse it for the costs of cleaning up a site may be dischargeable, the same governmental agency's right to compel us to spend our money cleaning up the same site may not be discharged even though the financial impact to AWI would have been the same in both instances if the liability had not been discharged.

*Specific Events*

Upon emergence, AWI resolved its environmental liabilities at 45 sites through its Chapter 11 Case. The liabilities at 38 sites were resolved through the global environmental settlement ("Global Settlement") with the Department of Justice ("DOJ") and the U.S. Environmental Protection Agency ("EPA") with respect to CERCLA liability. The Global Settlement, which was approved by the Bankruptcy Court in October 2005 and further amended in July 2007, provided EPA an approved proof of claim in the amount of \$9.2 million, which included \$7.8 million with respect to the Peterson Puritan site. At one CERCLA site, however, AWI will continue to participate in the cleanup under a previously approved Consent Decree. In addition to the federal claims resolved by the Global Settlement, AWI's emergence from Chapter 11 also resolved its environmental liabilities with respect to claims asserted by the state and/or private parties at seven other sites.

AWI is subject to an order of the Oregon Department of Environmental Quality ("DEQ") to investigate and remediate hazardous substances present at its St. Helens, Oregon facility which was previously owned by Kaiser Gypsum Company, Inc. ("Kaiser") and then Owens Corning Fiberglas Corp. ("OC"). Costs and responsibilities for the remedial investigation and remedy design are being shared with Kaiser pursuant to an agreement between AWI and Kaiser. Contributions to these costs are also being made available by DEQ pursuant to its settlement with OC for OC's liabilities for the property.

DEQ subsequently approached AWI to perform investigations in Scappoose Bay adjacent to the St. Helens, Oregon facility. AWI has denied liability for any contamination in Scappoose Bay. However,

Armstrong World Industries, Inc., and Subsidiaries  
Notes to Consolidated Financial Statements  
(dollar amounts in millions)

Kaiser entered into an agreement with DEQ to conduct such investigations in the Bay and AWI and OC have cooperated with Kaiser and provided a portion of the funding for the investigation, without waiving any defenses to liability. AWI continues to deny all liability for any contamination of the adjacent bay. We are not currently able to estimate with reasonable certainty any amounts we may incur with respect to the bay, although it is possible that such amounts may be material.

During the first quarter of 2008, we received a Notice and Finding of Violation from the U.S. EPA, Region 6 and also a Notice of Enforcement from the Texas Commission on Environmental Quality, relating to air emissions from our Center, Texas hardwood flooring manufacturing facility. The Finding of Violation from the U.S. EPA has been resolved. We have reached an agreement with the state of Texas. However, documents signed by Texas have not yet been received. Both matters have been resolved with total settlement amounts under \$0.1 million.

*Summary of Financial Position*

Liabilities of \$6.5 million and \$7.0 million at December 31, 2008 and December 31, 2007, respectively, were for potential environmental liabilities that we consider probable and for which a reasonable estimate of the probable liability could be made. Where existing data is sufficient to estimate the liability, that estimate has been used; where only a range of probable liabilities is available and no amount within that range is more likely than any other, the lower end of the range has been used. As assessments and remediation activities progress at each site, these liabilities are reviewed to reflect new information as it becomes available. These liabilities are undiscounted.

The estimated liabilities above do not take into account any claims for recoveries from insurance or third parties. In the fourth quarter of 2008, AWI concluded a settlement with an insurance carrier and the U.S. EPA for the reimbursement of funds for environmental costs related to specific, identified sites. This arrangement included a recovery by AWI from the carrier, a payment from AWI to the carrier for retrospective premiums and a payment from AWI to the EPA. This matter has been concluded, and we recorded a gain of \$6.9 million within SG&A during the fourth quarter of 2008. It is our policy to record probable recoveries that are either available through settlement or anticipated to be recovered through negotiation or litigation, as assets in the Consolidated Balance Sheets. The amount of the recorded asset for estimated recoveries was zero and \$2.1 million at December 31, 2008 and December 31, 2007, respectively.

Actual costs to be incurred at identified sites may vary from our estimates. Based on our current knowledge of the identified sites, we are not able to estimate with reasonable certainty future costs which may exceed amounts already recognized.

PATENT INFRINGEMENT CLAIMS

We are a defendant in a lawsuit claiming patent infringement related to some of our laminate flooring products. We are being defended and indemnified by our supplier for costs and potential damages related to the litigation. The jury verdict has held the asserted patent claims to be non-infringed and invalid for a number of reasons. The plaintiff has filed an appeal.

In the second quarter of 2007, a second lawsuit claiming patent infringement related to some of our laminate flooring products was settled without cost to us. We obtained a release with respect to past damages accruing up to June 30, 2008. Pursuant to its indemnity obligations, our supplier bore the costs of the litigation. With respect to certain laminate flooring products manufactured for AWI since July 1, 2008, the prior claims could be reasserted with full availability to AWI of all defenses previously raised. In such a case, AWI is the beneficiary of limited indemnities for litigation costs and potential damages.

During the first quarter of 2006, a favorable settlement of a patent infringement case totaling \$8.6 million was recorded within SG&A expenses. This case, in which we were the plaintiff, related to a previously divested business. We received the proceeds in the second quarter of 2006.



Armstrong World Industries, Inc., and Subsidiaries  
Notes to Consolidated Financial Statements  
(dollar amounts in millions)

OTHER CLAIMS

Additionally, we are involved in various other claims and legal actions involving product liability, patent infringement, breach of contract, distributor termination, employment law issues and other actions arising in the ordinary course of business. While complete assurance cannot be given to the outcome of these claims, we do not believe there is a reasonable possibility that a loss exceeding amounts already recognized would be material.

NOTE 33. EARNINGS PER SHARE

The difference between the average number of basic and diluted common shares outstanding is due to contingently issuable shares. Earnings per share components may not add due to rounding.

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

Not applicable.

**ITEM 9A. CONTROLS AND PROCEDURES**

Our management, with the participation of our chief executive officer and our chief financial officer, performed an evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 ("Exchange Act")) as of the end of the period covered by this Annual Report on Form 10-K. Our chief executive officer and our chief financial officer have concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed in reports we file or submit under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (2) accumulated and communicated to our management, including our chief executive officer and our chief financial officer, to allow their timely decisions regarding required disclosure.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended December 31, 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Management's Report on Internal Control over Financial Reporting and the Report of Independent Registered Public Accounting Firm are incorporated by reference to Item 8.

**ITEM 9B. OTHER INFORMATION**

On February 24, 2009 Stephen J. Senkowski, executive vice president and chief executive officer of Armstrong Building Products & Asia-Pacific Operations, announced he will retire effective April 1, 2009. He will be succeeded by F. Nicholas Grasberger III, who joined Armstrong as senior vice president and chief financial officer in 2005. An interim chief financial officer will be named shortly.

The Board of Directors established Monday, June 22, 2009 as the date for the Company's annual meeting of shareholders. Shareholders of record at the close of trading on March 27, 2009 will be entitled to vote at that meeting. Pursuant to Article II, Section 5 of the Company's Bylaws, if a shareholder other than the Asbestos Personal Injury Settlement Trust should wish to propose business to come before that meeting, written notice of such business must be received by the Corporate Secretary of the Company no later than March 25, 2009. Any such notice should be addressed to the attention of: Jeffrey D. Nickel, Corporate Secretary, Armstrong World Industries, Inc., 2500 Columbia Avenue, Lancaster, PA 17603. It is recommended that any notice be sent via means that will provide confirmation of the delivery date.

PART III

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

The information required by Item 10, other than information regarding the executive officers of the Company which is presented in Item 4A. Executive Officers of the Company, is incorporated by reference to the sections entitled “Code of Ethics,” “Board of Directors,” “Nominating and Governance Committee,” “Audit Committee and Audit Committee Expert,” “Management Development and Compensation Committee,” “Director Information” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Company’s proxy statement for its 2009 annual meeting of shareholders.

**ITEM 11. EXECUTIVE COMPENSATION**

The information required by Item 11 is incorporated by reference to the sections entitled “Compensation Discussion and Analysis,” “Compensation Committee Report,” “Summary Compensation Table,” “Grants of Plan-Based Awards,” “Outstanding Equity Awards at Fiscal Year-End,” “Option Exercises and Stock Vested,” “Pension Benefits,” “Nonqualified Deferred Compensation,” “Potential Payments Upon Termination or Change in Control,” “Compensation Committee Interlocks and Insider Participation” and “Compensation of Directors” in the Company’s proxy statement for its 2009 annual meeting of shareholders.

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

The information required by Item 12 is incorporated by reference to the sections entitled “Security Ownership of Certain Beneficial Owners,” “Security Ownership of Management” and “Equity Compensation Plan Information” in the Company’s proxy statement for its 2009 annual meeting of shareholders.

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

The information required by Item 13 is incorporated by reference to the sections entitled “Certain Relationships and Related Transactions” and “Director Independence” in the Company’s proxy statement for its 2009 annual meeting of shareholders.

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

The information required by Item 14 is incorporated by reference to the section entitled “Audit Committee Report” in the Company’s proxy statement for its 2009 annual meeting of shareholders.

PART IV

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

(a) Listing of Documents

1. The financial statements and schedule of Armstrong World Industries, Inc. filed as a part of this 2008 Annual Report on Form 10-K is listed in the "Index to Financial Statements and Schedules" on page 52.
2. The financial statements required to be filed pursuant to Item 15 of Form 10-K are:  
 Worthington Armstrong Venture consolidated financial statements for the years ended December 31, 2008, 2007 and 2006 (filed herewith as Exhibit 99)
3. The following exhibits are filed as part of this 2008 Annual Report on Form 10-K:

Exhibit No.	Description
No. 2	Armstrong World Industries, Inc.'s Fourth Amended Plan of Reorganization, as amended by modifications through May 23, 2006 is incorporated by reference from the 2005 Annual Report on Form 10-K wherein it appeared as Exhibit 2.3.
No. 3.1	Amended and Restated Certificate of Incorporation of Armstrong World Industries, Inc. is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 3.1.
No. 3.2	Armstrong World Industries, Inc.'s Bylaws are incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein they appeared as Exhibit 3.2.
No. 10.1	Management Achievement Plan for Key Executives, effective as of November 28, 1983, as amended April 30, 2007 and December 8, 2008, is filed with this Report. *
No. 10.2	Retirement Benefit Equity Plan, effective January 1, 2005, as amended October 29, 2007 and December 8, 2008 is filed with this Report. *
No. 10.3	Bonus Replacement Retirement Plan, effective as of January 1, 1998, as amended January 1, 2007, is incorporated by reference from the 2007 Annual Report on Form 10-K wherein it appeared as Exhibit 10.9.*
No. 10.4	Employment Agreement with Michael D. Lockhart, as amended, is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended September 30, 2008, wherein it appeared as Exhibit 10.8. *
No. 10.5	Hiring Agreement with F. Nicholas Grasberger III dated January 6, 2005 is incorporated by reference from the Current Report filed on Form 8-K/A on January 6, 2005, wherein it appeared as Exhibit 10.1. *
No. 10.6	Indemnification Agreement with F. Nicholas Grasberger III dated January 6, 2005 is incorporated by reference from the Current Report filed on Form 8-K/A on January 6, 2005, wherein it appeared as Exhibit 10.3. *

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<u>Exhibit No.</u>	<u>Description</u>
No. 10.7	Armstrong World Industries, Inc.'s Nonqualified Deferred Compensation Plan effective January 2005 is incorporated by reference from the 2005 Annual Report on Form 10-K wherein it appeared as Exhibit 10.29. *
No. 10.8	Schedule of Armstrong World Industries, Inc. Nonemployee Director Compensation is incorporated by reference from the 2006 Annual Report on Form 10-K wherein it appeared as Exhibit 10.19. *
No. 10.9	Indemnification Agreement with Donald A. McCuniff dated March 13, 2006 is incorporated by reference from the Current Report filed on Form 8-K on March 14, 2006, wherein it appeared as Exhibit 10.2. *
No. 10.10	Credit Agreement, dated as of October 2, 2006, by and among the Company, certain subsidiaries of the Company as guarantors, Bank of America, N.A., as Administrative Agent, the other lenders party thereto, JP Morgan Chase Bank, N.A. and Barclays Bank PLC, as Co-Syndication Agents and LaSalle Bank National Association and the Bank of Nova Scotia, as Co-Documentation Agents, is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 10.1.
No. 10.11	The Armstrong World Industries, Inc. Asbestos Personal Injury Settlement Trust Agreement dated as of October 2, 2006, by and among Armstrong World Industries, Inc. and, as trustees, Anne M. Ferazzi, Harry Huges, Paul A. Knuti, Lewis R. Sifford and Thomas M. Tully is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 10.2.
No. 10.12	Stockholder and Registration Rights Agreement, dated as of October 2, 2006, by and between Armstrong World Industries, Inc. and the Armstrong World Industries, Inc. Asbestos Personal Injury Asbestos Trust is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 10.3.
No. 10.13	Armstrong World Industries, Inc. 2006 Long-Term Incentive Plan, as amended February 23, 2009, is filed with this Report. *
No. 10.14	Form of Armstrong World Industries, Inc. 2006 Long-Term Incentive Plan Stock Option Agreement is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 10.5. *
No. 10.15	Form of Armstrong World Industries, Inc. 2006 Long-Term Incentive Plan Restricted Stock Award Agreement is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 10.6. *
No. 10.16	Form of Armstrong World Industries, Inc. 2006 Long-Term Incentive Plan notice of restricted stock and/or option award is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 10.7. *
No. 10.17	Form of Indemnification Agreement for directors and officers of Armstrong World Industries, Inc. is incorporated by reference from the Current Report on Form 8-K dated October 2, 2006, wherein it appeared as Exhibit 10.8. * A Schedule of Participating Directors and Officers is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended June 30, 2008 wherein it appeared as Exhibit 10.28.
No. 10.18	2006 Phantom Stock Unit Plan as amended December 8, 2008, is filed with this Report. *

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<u>Exhibit No.</u>	<u>Description</u>
No. 10.19	2006 Phantom Stock Unit Agreement is incorporated by reference from the Current Report on Form 8-K dated October 23, 2006, wherein it appeared as Exhibit 10.3. A Schedule of Participating Directors is incorporated by reference from the 2006 Annual Report on Form 10-K wherein it appeared as Exhibit 10.36. *
No. 10.20	2007 Award under the 2006 Phantom Stock Unit Agreement and the Schedule of Participating Directors are incorporated by reference from the Current Report on Form 8-K dated October 22, 2007, wherein they appeared as Exhibits 10.1 and 10.2, respectively. *
No. 10.21	Stipulation and Agreement with Respect to Claims of Armstrong Holdings, Inc. and Armstrong Worldwide, Inc.; and Motion for Order Approving Stipulation and Agreement are incorporated by reference from the Current Report on Form 8-K dated February 26, 2007, wherein they appeared as Exhibits 99.2 and 99.3, respectively.
No. 10.22	Share Purchase Agreement dated March 27, 2007, between the Company and NPM Capital N.V. and Flagstone Beheer B.V. for the sale of Tapijtfabriek H. Desseaux N.V. and its subsidiaries is incorporated by reference from the 2006 Annual Report on Form 10-K wherein it appeared as Exhibit 10.38.
No. 10.23	Form of Armstrong World Industries, Inc. grant letter used in connection with the equity grant of stock options and performance restricted shares under the 2006 Long-Term Incentive Plan to Michael D. Lockhart is incorporated by reference from the 2007 Annual Report on Form 10-K wherein it appeared as Exhibit 10.34. *
No. 10.24	Form of Armstrong World Industries, Inc. grant letter used in connection with awards of restricted stock under the 2006 Long-Term Incentive Plan is incorporated by reference from the 2007 Annual Report on Form 10-K wherein it appeared as Exhibit 10.35. *
No. 10.25	Amendment No. 1, dated February 25, 2008, to the Credit Agreement, dated October 2, 2006, by and among the Company, certain subsidiaries of the Company as guarantors, Bank of America, N.A., as Administrative Agent, the other lenders party thereto, JP Morgan Chase Bank, N.A. and Barclays Bank PLC, as Co-Syndication Agents and LaSalle Bank National Association and the Bank of Nova Scotia, as Co-Documentation Agents, is incorporated by reference from the 2007 Annual Report on Form 10-K wherein it appeared as Exhibit 10.36.
No. 10.26	Form of Armstrong World Industries, Inc. grant letter used in connection with award of stock options under the 2006 Long-Term Incentive Plan is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended March 31, 2008 wherein it appeared as Exhibit 10.37. *
No. 10.27	2008 Directors Stock Unit Plan as amended December 8, 2008 is filed with this Report. *
No. 10.28	Form of 2008 Service Commencement Award to each of Stan A. Askren and Jon A. Boscia is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended September 30, 2008 wherein it appeared as Exhibit 10.34. *
No. 10.29	Form of 2008 Award under the 2008 Director Stock Unit Plan is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended September 30, 2008 wherein it appeared as Exhibit 10.35. *
No. 10.30	Schedule of Participating Directors to the 2008 award under the 2008 Directors Stock Unit Plan is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended September 30, 2008 wherein it appeared as Exhibit 10.36. *

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<u>Exhibit No.</u>	<u>Description</u>
No. 10.31	Form of Change in Control Agreement with certain officers is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended September 30, 2008 wherein it appeared as Exhibit 10.37. *
No. 10.32	Schedule of Participating Officers to the Form of Change in Control Agreement is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended September 30, 2008 wherein it appeared as Exhibit 10.38. *
No. 10.33	Form of Change in Control Agreement with Michael D. Lockhart is incorporated by reference from the Quarterly Report on Form 10-Q for the quarter ended September 30, 2008 wherein it appeared as Exhibit 10.39. *
No. 11	Computation of Earnings Per Share.
No. 21	Armstrong World Industries, Inc.'s Subsidiaries.
No. 23.1	Consent of Independent Registered Public Accounting Firm.
No. 23.2	Consent of Independent Registered Public Accounting Firm.
No. 24	Power of Attorney and Authorizing Resolution.
No. 31.1	Certification of Principal Executive Officer required by Rule 13a-15(e) or 15d-15(e) of the Securities Exchange Act.
No. 31.2	Certification of Principal Financial Officer required by Rule 13a-15(e) or 15d-15(e) of the Securities Exchange Act.
No. 32.1	Certification of Chief Executive Officer required by Rule 13a and 18 U.S.C. Section 1350 (furnished herewith).
No. 32.2	Certification of Chief Financial Officer required by Rule 13a and 18 U.S.C. Section 1350 (furnished herewith).
No. 99	Worthington Armstrong Venture consolidated financial statements for years ended December 31, 2008, 2007, and 2006.
*	Management Contract or Compensatory Plan.

SIGNATURES

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

ARMSTRONG WORLD INDUSTRIES, INC.  
(Registrant)

By: /s/ Michael D. Lockhart  
Chairman and Chief Executive Officer

Date: February 26, 2009

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this Report has been signed below by the following persons on behalf of the registrant Armstrong and in the capacities and on the dates indicated.

Directors and Principal Officers of the registrant AWI:

<u>Name</u>	<u>Title</u>
Michael D. Lockhart	Chairman and Chief Executive Officer (Principal Executive Officer)
F. Nicholas Grasberger III	Senior Vice President and Chief Financial Officer (Principal Financial Officer)
Stephen F. McNamara	Vice President and Controller (Chief Accounting Officer)
Stanley A. Askren	Director
Jon A. Boscia	Director
James J. Gaffney	Director
Robert C. Garland	Director
Judith R. Haberkorn	Director
James J. O'Connor	Director
Russell F. Peppet	Director
Arthur J. Pergament	Director
John J. Roberts	Director
Alexander M. Sanders, Jr.	Director

By: /s/ Michael D. Lockhart  
(Michael D. Lockhart, as attorney-in-fact  
for AWI directors and on his own behalf)  
As of February 26, 2009

By: /s/ F. Nicholas Grasberger III  
(F. Nicholas Grasberger III)  
As of February 26, 2009

By: /s/ Stephen F. McNamara  
(Stephen F. McNamara)  
As of February 26, 2009





## SCHEDULE II

Armstrong World Industries, Inc.  
Valuation and Qualifying Reserves of Accounts Receivable  
(amounts in millions)

	Successor Company			Predecessor Company
	Year Ended December 31, 2008	Year Ended December 31, 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
<b>Provision for Losses</b>				
Balance at beginning of period	\$ 11.8	\$ 10.6	\$ 10.8	\$ 10.8
Additions charged to earnings	8.6	10.3	1.4	5.2
Deductions	(9.6)	(9.1)	(1.6)	(4.1)
Discontinued operations	—	—	—	(1.1)
Balance at end of period	<u>\$ 10.8</u>	<u>\$ 11.8</u>	<u>\$ 10.6</u>	<u>\$ 10.8</u>
<b>Provision for Discounts and Warranties</b>				
Balance at beginning of period	\$ 51.9	\$ 56.2	\$ 54.3	\$ 44.0
Additions charged to earnings	225.6	228.6	51.0	192.6
Deductions	(233.8)	(232.9)	(49.1)	(182.3)
Balance at end of period	<u>\$ 43.7</u>	<u>\$ 51.9</u>	<u>\$ 56.2</u>	<u>\$ 54.3</u>
<b>Total Provision for Discounts, Warranties and Losses</b>				
Balance at beginning of period	\$ 63.7	\$ 66.8	\$ 65.1	\$ 54.8
Additions charged to earnings	234.2	238.9	52.4	197.8
Deductions	(243.4)	(242.0)	(50.7)	(186.4)
Discontinued operations	—	—	—	(1.1)
Balance at end of period	<u>\$ 54.5</u>	<u>\$ 63.7</u>	<u>\$ 66.8</u>	<u>\$ 65.1</u>

Exhibit Index

Exhibit No.

No. 10.1	Management Achievement Plan for Key Executives, effective as of November 28, 1983, as amended April 30, 2007 and December 8, 2008.
No. 10.2	Retirement Benefit Equity Plan, effective January 1, 2005, as amended October 29, 2007 and December 8, 2008.
No. 10.13	Armstrong World Industries, Inc. 2006 Long-Term Incentive Plan, as amended February 23, 2009.
No. 10.18	2006 Phantom Stock Unit Plan, as amended December 8, 2008.
No. 10.27	2008 Directors Stock Unit Plan, as amended December 8, 2008.
No. 11	Computation of Earnings Per Share.
No. 21	Armstrong World Industries, Inc.'s Subsidiaries.
No. 23.1	Consent of Independent Registered Public Accounting Firm.
No. 23.2	Consent of Independent Registered Public Accounting Firm.
No. 24	Power of Attorney and Authorizing Resolution.
No. 31.1	Certification of Principal Executive Officer required by Rule 13a-15(e) or 15d-15(e) of the Exchange Act.
No. 31.2	Certification of Principal Financial Officer required by Rule 13a-15(e) or 15d-15(e) of the Exchange Act.
No. 32.1	Certification of Chief Executive Officer required by Rule 13a and 18 U.S.C. Section 1350.
No. 32.2	Certification of Chief Financial Officer required by Rule 13a and 18 U.S.C. Section 1350.
No. 99	Worthington Armstrong Venture consolidated financial statements as of December 31, 2008 and 2007 and for the years ended December 31, 2008, 2007 and 2006.

**MANAGEMENT ACHIEVEMENT PLAN**  
**PLAN TEXT AND ADMINISTRATIVE GUIDELINES**  
**ADOPTED BY BOARD OF DIRECTORS**  
**NOVEMBER 28, 1983**  
AS AMENDED DECEMBER 8, 2008

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ARMSTRONG WORLD INDUSTRIES, INC.

MANAGEMENT ACHIEVEMENT PLAN FOR KEY EXECUTIVES

AMENDED DECEMBER 8, 2008

(PLAN TEXT)

1. Purpose

The Armstrong World Industries, Inc. (the “Company”) Management Achievement Plan (the “Plan”) is designed to promote the financial success of the Company by recognizing the significant contributions key employees can make to the achievement of Company goals. The Plan’s objectives are to motivate key Company and subsidiary employees to produce outstanding results by providing the opportunity to earn financial rewards in relation to the attainment of corporate, business unit and individual goals.

The Plan is based on the concept that the Company establishes for each participant at the beginning of the year a target incentive award based on the achievement of specific corporate, business unit and individual goals. When the year is over, the results actually achieved will be evaluated against these goals to determine the amount, if any, of compensation that may be paid to individuals participating in the Plan.

2. Administration

The Plan shall be administered by the Management Development and Compensation Committee (the “Committee”) of the Board of Directors of the Company with the advice and counsel of its Chief Executive Officer. Designated subsidiary companies may adopt this Plan. Subject to compliance with the requirements of Section 162(m) of the Internal Revenue Code for deductibility of awards, the Board may amend or terminate the Plan from time to time so long as the amendment or termination does not adversely affect any rights or obligations with respect to awards for the then-current year or any prior year which has not yet been paid.

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3. Eligibility

The intent of the Plan is to extend participation only to those key employees whose duties and responsibilities give them the opportunity to make a continuing material and substantial impact on the achievement of organization goals. The Chief Executive Officer of the Company may annually determine the non-executive officer participants and recommend executive officer participants to the Committee.

4. Incentive Awards

- A) At the beginning of each year, the Chief Executive Officer shall present to the Committee criteria for evaluating performance against corporate and business unit goals for the purposes of determining the level of incentive awards which may be paid for the year based upon actual results for the year.
- B) At the same time, the Chief Executive Officer shall recommend a target award expressed as a percentage of salary for each participant which shall be subject to approval by the Committee.
- C) As soon as practical following the close of each year, the Chief Executive Officer shall evaluate the levels of corporate and business unit achievement and individual performance. Based on these factors, the Chief Executive Officer shall recommend to the Committee the percentage of the target award to be paid to each participant based on corporate and business unit results. Following the receipt of the recommendations from the Chief Executive Officer, the Committee shall determine the amount to be paid to participants based on corporate and business unit results. The maximum bonus achievement percentage for corporate and business unit performance shall be 200% of the target award. Within parameters established by the Committee, the Chief Executive Officer may increase or decrease the award payments for non-executive officer participants based on the Company's evaluation of their individual performance. The award payments for executive officer participants shall be approved by the Committee. All award payments authorized by the Committee will be final.
- D) The performance measures approved by the shareholders for determining awards under the Plan are: cash flow, earnings, operating income and sales. The Committee has established \$3 million as the maximum amount that may be paid to any participant in any one year under the Plan.

- E) The incentive award determined in accordance with the provisions of Paragraphs A through D of this Section 4 shall be reduced for such year as follows for Plan participants who are eligible to participate in the Bonus Replacement Retirement Plan of Armstrong World Industries, Inc.:
- (1) If a Plan participant's grade level is 18 or 19 as of January 1 of the calendar year for which the incentive award is determined, the incentive award otherwise payable shall be reduced by the lesser of (i) 50% of the amount determined under Paragraphs A through D, (ii) \$7,500 or (iii) the authorized contribution to the Bonus Replacement Retirement Plan.
  - (2) If a Plan participant's grade level is 20 or 21 as of January 1 of the calendar year for which the incentive award is determined, the incentive award otherwise payable shall be reduced by the lesser of (i) 50% of the amount determined under Paragraphs A through D, (ii) \$15,000 or (iii) the authorized contribution to the Bonus Replacement Retirement Plan.
  - (3) If a Plan participant's grade level is 22 or higher as of January 1 of the calendar year for which the incentive award is determined, the incentive award otherwise payable shall be reduced by the lesser of (i) 50% of the amount determined under Paragraphs A through D, (ii) \$20,000 or (iii) the authorized contribution to the Bonus Replacement Retirement Plan.

5. Time of Payment

Awards under this Plan shall be paid as soon as practicable after the yearly financial results have been determined.

6. Miscellaneous Provisions

- A) Condition of Award — Plan participants who retire, become disabled, die or are involuntarily terminated for reasons other than cause on or after the last workday of March may be eligible for a prorated award based on the Company's evaluation of their individual performance. Employees who voluntarily terminate employment at any time from the beginning of the year until the award for that year is paid are not eligible for an award. The Committee, in its absolute discretion, may determine to direct payment of all or any portion of an award to an individual notwithstanding the preceding two sentences.
- B) No Assignment or Transfer — Awards are payable only to the participant, except in the case of death or legal incapacity at the time of payment, the award may be paid to his heirs, estate or legal guardian. No awards under the Plan or any rights or interests therein shall be assignable or transferable by a participant.
- C) No Rights to Awards — No employee or other person shall have any claim or right to be granted an award under the Plan. Neither the Plan nor any action taken hereunder shall be construed as giving any employee any right to be retained in the employ of the Company or any of its subsidiaries.
- D) Withholding Taxes — The Company shall have the right to deduct from all awards hereunder paid all taxes required by law to be withheld with respect to such awards.



- E) Funding of Plan — The Company shall not be required to establish any special or separate fund or to make any other segregation of assets to assure the payment of any award under the Plan.
- F) Change in Control Payment Provisions — In the event of a sale, merger or consolidation of the Company which occurs prior to December 31 of any Plan year and results in a change in control of the Company (as defined in the Company's 2006 Long-Term Incentive Plan and any successor plan), Plan participants shall be paid a lump sum payment equal to each participant's pro-rated target award. The payment amount will be the participant's eligible base salary earnings for the time worked from the start of the performance period to the date of the change in control multiplied by the target bonus award percentage. Cash payments will be made as soon as practical following the date of the change in control. Payments made under this Paragraph F shall cause the Plan performance to be completed as of the date of the change in control which triggered the payment.

7. Effective Date of the Plan

The effective date of the Plan shall be November 28, 1983.

As Amended December 8, 2008,  
effective as of January 1, 2005

**RETIREMENT BENEFIT EQUITY PLAN  
OF  
ARMSTRONG WORLD INDUSTRIES, INC.**

This Retirement Benefit Equity Plan was originally established, pursuant to the authority of the Board of Directors of Armstrong World Industries, Inc., effective January 1, 1976 to pay supplemental retirement benefits to certain employees of the Company who have qualified or may qualify for benefits under the Retirement Income Plan for Employees of Armstrong World Industries, Inc. The Retirement Benefit Equity Plan was previously amended and restated as of March 1, 2004.

The Retirement Benefit Equity Plan is hereby amended and restated as of January 1, 2005 to comply with the requirements of Section 409A of the Internal Revenue Code of 1986 as amended and the guidance (including transitional guidance) thereunder.

All benefits payable under this Plan shall be paid out of the general assets of the Company, or from a trust, if any, established by the Company for the purpose of paying benefits under the Plan, the assets of which shall remain subject to the claims of judgment creditors of the Company in accordance with the provisions of any such trust.

Article 1. Definitions

- 1.01. "Actuarial Equivalent Present Value" shall refer to the present value of a Member's supplemental benefits. With respect to any Member who is eligible to retire or has retired under the Retirement Income Plan, such present value shall be determined using the actuarial assumptions and factors reasonably utilized under the Retirement Income Plan as of the date of determination applied to a single life annuity payable immediately. With respect to any Member who is not eligible to retire or has not retired under the Retirement Income Plan, such present value shall be determined using the actuarial assumptions and factors reasonably utilized under the Retirement Income Plan as of the date of determination applied to an age 65 single life annuity. The determination of Actuarial Equivalent Present Value shall reflect future assumed increases in the limitations under Section 415 of the Internal Revenue Code, with such future assumed increases being based on the interest rate that is used by the Committee to determine the amount of any employment taxes that may be owed under Section 3121(v) of the Internal Revenue Code.
  - 1.02. "Board of Directors" shall mean the Board of Directors of the Company.
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- 1.03. "Change in Control" shall mean the first to occur of any of the following events: (i) a Change in Ownership of the Company, (ii) a Change in Effective Control of the Company or (iii) a Change in the Ownership of a Substantial Portion of the Assets of the Company.
- (a) A "Change in Ownership" of the Company occurs on the date that any one person, or more than one person acting as a group acquires ownership of stock of the Company that, together with stock held by such person or group, constitutes more than 50 percent of the total fair market value or total voting power of the stock of the Company.
  - (b) A "Change in Effective Control" of the Company occurs on the date that either:
    - (i) Any one person, or more than one person acting as a group, acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) ownership of stock of the Company possessing 30 percent or more of the total voting power of the stock of the Company; or
    - (ii) a majority of members of the Company's board of directors is replaced during any 12-month period by directors whose appointment or election is not endorsed by a majority of the members of the Company's board of directors prior to the date of the appointment or election.
  - (c) A "Change in the Ownership of a Substantial Portion of the Assets of the Company" occurs on the date that any one person, or more than one person acting as a group, acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) assets from the Company that have a total gross fair market value equal to or more than 40 percent of the total gross fair market value of all of the assets of the Company immediately prior to such acquisition or acquisitions. For this purpose, gross fair market value means the value of the assets being disposed of, determined without regard to any liabilities associated with such assets. There is no Change in Control event under this Section 1.03(c) when there is a transfer to an entity that is controlled by the shareholders of the transferring corporation immediately after the transfer.

The determination of whether a Change in Control event has occurred will be made in accordance with the requirements of Code Section 409A and the guidance issued thereunder. The foregoing definition of Change in Control shall exclude the occurrence of the date(s) on which (i) the Chapter 11 Plan of Reorganization of the Company shall become effective and (ii) the creation by the Company of the Asbestos Personal Injury Trust.

1.04. "Committee" shall mean the Retirement Committee as provided for in Article 4.

1.05. "Company" shall mean Armstrong World Industries, Inc. or any successor by merger, purchase or otherwise, with respect to its employees. The term Company shall also mean any other company participating in the Retirement Income Plan with respect to its employees if such Company adopts this Plan.

- 1.06. "Compensation" shall mean a Member's "compensation" as determined under the Retirement Income Plan without regard to limitations under Section 401(a)(17) of the Internal Revenue Code, plus amounts deferred by the Member under the Armstrong Deferred Compensation Plan, if any, and amounts contributed by the Company to the Bonus Replacement Retirement Plan of Armstrong World Industries, Inc. (the "Bonus Replacement Retirement Plan") on behalf of the Member in the year in which such contribution is made.
- 1.07. "Effective Date" shall mean January 1, 1976.
- 1.08. "Member" shall mean any person included in the membership of the Plan as provided in Article 2.
- 1.09. "Plan" shall mean the Retirement Benefit Equity Plan of Armstrong World Industries, Inc. as described herein or as hereafter amended.
- 1.10. "Specified Employee" shall mean, as determined pursuant to Section 409A of the Internal Revenue Code and regulations thereunder, a key employee (as defined in Section 416(i) of the Code without regard to paragraph 5 thereof) of the Company if any stock of the Company is publicly traded on an established securities market or otherwise.
- 1.11. "Retirement Income Plan" shall mean the Retirement Income Plan for Employees of Armstrong World Industries, Inc. as amended and restated as of January 1, 2007 as may be amended from time to time.

## Article 2. Membership

- 2.01. Every person who was a member of the Plan as in effect on December 31, 1999 shall remain a Member of the Plan on or after January 1, 2000.
- 2.02. Every other employee of the Company shall become a Member of the Plan on the first day of the calendar year in which the Committee determines that:
  - (a) the employee's benefit calculated under the Retirement Income Plan exceeds the allowed benefit under Section 415 of the Internal Revenue Code,
  - (b) the employee's compensation exceeds the maximum allowed under Section 401(a)(17) of the Internal Revenue Code,
  - (c) the employee has compensation deferred under the terms of the Armstrong Deferred Compensation Plan,

- (d) the employee is a key executive designated by the Board of Directors, or its delegate, to receive credit for employment prior to his Company employment for purposes of calculating his Retirement Income Plan benefit, as provided under Section 3.01(a)(iii) of this Plan, or
- (e) the employee has a contribution made on his behalf to the Bonus Replacement Retirement Plan.

Effective January 1, 2008, every other employee of the Company shall become a Member of the Plan on the first day of the calendar year following the calendar year in which the Committee makes the determination described above.

- 2.03. Membership under the Plan shall terminate if a Member's employment with the Company terminates unless at that time the Member is entitled to retirement income payments pursuant to the Retirement Income Plan or benefits described in Section 3.04.

### Article 3. Amount and Payment of Supplemental Benefits

- 3.01. The supplemental benefits under this Plan shall be payable by the Company only with respect to a Member who has retired or otherwise terminated his employment with the Company after becoming vested under the Retirement Income Plan. Any such supplemental benefits shall be payable from the general assets of the Company or from a trust, if any, established by the Company for the purpose of paying benefits under the Plan, the assets of which shall remain subject to the claims of judgment creditors of the Company in accordance with the provisions of any such trust.

The amount of any supplemental benefits payable to a Member pursuant to this Plan, expressed as a single life annuity payable as of the Member's "normal retirement date" (as that term is defined in the Retirement Income Plan) or in the event the Member defers his retirement beyond his normal retirement date, his "deferred retirement date" (as that term is defined in the Retirement Income Plan), shall be equal to (a) minus (b) minus (c) minus (d), where:

- (a) is the benefit calculated under the provisions of the Retirement Income Plan, but:
  - (i) disregarding any reduction in the amount of benefits under the Retirement Income Plan attributable to any provision therein incorporating limitations imposed by Section 415 of the Internal Revenue Code or Section 401(a)(17) of the Internal Revenue Code;
  - (ii) disregarding any reduction due to compensation deferred under the Armstrong Deferred Compensation Plan;
  - (iii) including, for purposes of calculating Total Service under the Retirement Income Plan, years of employment for a Member described in Section 2.02(d) which precede his Company employment to the extent so designated by the Board of Directors, or its delegate, at the time such individual is designated as eligible for membership in the Plan; and

- (iv) including, for purposes of determining compensation, any amounts contributed on the Member's behalf to the Bonus Replacement Retirement Plan; and
  - (v) excluding any amount attributable to (1) an Extraordinary Event (as defined in the Retirement Income Plan) and (2) all retirement enhancements related to past and future service that may become payable due to a job loss following a Change in Control (as defined in the Retirement Income Plan) under the Retirement Income Plan.
- (b) is the actual amount of benefits payable to or on account of the Member as calculated under the Retirement Income Plan, excluding any amounts attributable to (1) an Extraordinary Event (as defined in the Retirement Income Plan) and (2) all retirement enhancements related to past and future service that may become payable due to a job loss following a Change in Control (as defined in the Retirement Income Plan) under the Retirement Income Plan;
- (c) is the value of the benefit (excluding the portion of such benefit attributable to employee contributions) which is payable, which has been paid or which will become payable to a Member described in Section 2.02(d) from a qualified defined benefit plan to the extent such plan takes into account the period of employment described in Section 3.01(a)(iii). In the event the Member has received, is receiving, or is scheduled to receive benefits from another such plan in any form other than a single life annuity or at a time other than when benefits commence under this Plan, the benefit to be taken into account under this subsection (c) shall be determined by the Company based on actuarial assumptions and factors reasonably utilized under the Retirement Income Plan as of the date of determination; and
- (d) is the actuarial equivalent value of any supplemental benefits previously paid to the Member under this Plan, provided that the actuarial equivalent value of any supplemental benefits paid as a single sum shall be determined using the actuarial assumptions and factors reasonably utilized under the Retirement Income Plan as of the date of determination.

Notwithstanding the preceding provisions of this Section 3.01, in the event a retired or terminated Member's benefit calculated under the Retirement Income Plan is increased for any reason after the Member's supplemental benefit payments have commenced in an annuity form, the amount of any supplemental benefits payable to or on account of such Member under this Plan shall be reduced correspondingly on a prospective basis, and in the event such increase is made retroactively resulting in the overpayments of any or all of the Member's supplemental benefits, future benefit payments under this Plan shall be reduced to reflect such prior overpayments in any manner determined by the Committee, in its discretion, and applied on a consistent basis to all similarly situated Members, until an amount equal to the total overpayments in the Member's supplemental benefit payments are recovered.

3.02. Subject to the following rules, an employee of the Company who becomes a Member under this Plan in accordance with Section 2.02 shall elect in writing the form and timing of payment of the supplemental benefits payable on behalf of such Member under this Plan within the thirty (30) day period following the Committee's determination that such employee has become a Member.

- (a) The Member may elect to have his supplemental benefits paid in the form of any annuity that is offered under the Retirement Income Plan (other than a level income life annuity or a level income joint and survivor annuity). Effective January 1, 2005, a Member may initially elect to have his benefit paid in the form of a "life annuity" and then, immediately prior to commencement of payment, elect the specific form of actuarially equivalent life annuity among those offered under the Retirement Income Plan.
- (b) In no event shall the Member elect to have his supplemental benefits commence or be paid earlier than the later of: (i) the Member's attainment of age 55, or (ii) the date the Member first becomes eligible to receive his benefits under the Retirement Income Plan and in no event shall the Member elect to have his supplemental benefits commence or be paid later than the Member's attainment of age 65 or, if later, his actual retirement from the Company.

In no event shall the Member elect to have his supplemental benefits commence to be paid later than April 1 of the calendar year following the later of (x) the calendar year in which the Member attains age 70 1/2, or (y) the calendar year in which the Member terminates employment.

- (c) In the event the Member fails to affirmatively elect the form and timing of payment of his supplemental benefits hereunder, the Member shall be deemed to have elected to have his supplemental benefits paid in the form and at the time that his benefits are paid under the Retirement Income Plan. Effective January 1, 2009, in the event the Member fails to affirmatively elect the form and timing of payment of his supplemental benefits hereunder, the Member shall be deemed to have elected to have his supplemental benefits paid in the form of a life annuity and at the later of the Member's attainment of age 55 or termination of employment.
- (d) Notwithstanding any other provision of the Plan to the contrary, in the event the Member elects to receive a period certain annuity or joint and survivor annuity and either the beneficiary designated by the Member dies prior to the date the Member commences receiving his supplemental benefits or the Member designates his spouse as his beneficiary and the Member is not legally married to such spouse immediately preceding the date the Member commences receiving his supplemental benefits, the Member's election to receive such period certain annuity or joint and survivor annuity shall automatically be converted to an election to receive a single life annuity.

- 3.03. Notwithstanding the provisions of Section 3.02, a Member who has not commenced receiving payment of his supplemental benefits may request in writing to the Committee to amend the commencement date of his supplemental benefits elected by the Member under Section 3.02, in accordance with the following rules:
- (a) A Member who has not commenced receiving payment of his supplemental benefits may request to amend the timing and/or form of payment of the supplemental benefits (subject to the limitations of Section 3.02(a)) provided: (i) the commencement date in the absence of such distribution election amendment is not within twelve (12) months of the date of the amendment; (ii) his amended commencement date is at least twelve (12) months (five (5) years for election amendments made on or after January 1, 2009) after the date of the distribution election amendment; (iii) for election amendments made on or after January 1, 2009, such election amendment will not take effect until twelve (12) months after the date it is received by the Committee; and (iv) his amended commencement date is otherwise in conformance with the provisions of Section 3.02(b). Notwithstanding the foregoing: (i) during calendar year 2007, a Member who has not yet commenced receiving payment of his supplemental benefits may request in writing to the Committee to amend the timing and/or form of payment (subject to the limitations of Section 3.02(a)) provided the amendment shall only apply to amounts that would not otherwise be payable in 2007 and shall not cause an amount to be paid in 2007 that would not otherwise be payable in 2007; and (ii) during calendar year 2008, a Member who has not yet commenced receiving payment of his supplemental benefits may request in writing to the Committee to amend the timing and/or form of payment (subject to the limitations of Section 3.02(a)) provided the amendment shall only apply to amounts that would not otherwise be payable in 2008 and shall not cause an amount to be paid in 2008 that would not otherwise be payable in 2008.
- 3.04. Notwithstanding the provisions of Section 3.01 and Section 3.02, supplemental benefits shall be payable under this Plan to or on account of a Member described in Section 2.02(d) who: (i) is involuntarily terminated after completing one year of service but prior to becoming vested in the Retirement Income Plan, and (ii) receives severance pay benefits under the Severance Pay Plan for Salaried Employees of Armstrong World Industries, Inc. or any individual severance agreement. The Member's supplemental benefits will be calculated using the guaranteed pension schedule for Salaried Employees of Armstrong World Industries, Inc. under the Retirement Income Plan multiplied by the total years of service credited for employment prior to his Company employment, as determined in Section 2.02(d) and his years of Company employment and shall be payable in the form of a single life annuity commencing as of the later of the Member's attainment of age 62 or the Member's termination date.



- 3.05. Effective for periods prior to January 1, 2005, if a Member is restored to employment with the Company after having retired, any monthly payments under the Plan shall be discontinued and, upon subsequent retirement or termination of employment with the Company, the Member's benefits under the Plan shall be recomputed in accordance with Section 3.01 and shall again become payable to such Member in accordance with the provisions of the Plan, including his election under Section 3.02.
- 3.06. In the event the dollar amount of the maximum benefit under the Retirement Income Plan pursuant to Section 415 of the Internal Revenue Code increases because of adjustments in the cost of living, the supplemental benefits of any Member payable under the Plan, whether or not in pay status, shall be recalculated to take into account the higher maximum benefit payable from the Retirement Income Plan. If payments have already commenced under the Retirement Income Plan and this Plan, benefit amounts under both plans shall be adjusted to reflect the higher maximum benefit, by increasing the amount paid under the Retirement Income Plan and decreasing the amount paid under this Plan, as soon as administratively possible after such a change. Notwithstanding the above, if the Retirement Income Plan is terminated, no adjustments shall be made to benefits payable under this Plan with respect to changes in the maximum benefit after the date of such termination.
- 3.07. In the event a Member dies after becoming vested under the Retirement Income Plan but prior to the date his supplemental benefits under this Plan are scheduled to commence or be paid, a spouse's benefit shall be payable to the Member's surviving spouse. The spouse's benefit shall be paid to the Member's surviving spouse in a life annuity, beginning as of the first day of the month immediately following the date of the Member's death or, if later, the date the Member would have attained age 55 if he had lived, under which each payment shall equal one-half ( $\frac{1}{2}$ ) of the amount that would have been payable to the Member under Section 3.01 if the Member had elected a single life annuity under Section 3.02 with payments commencing as of the same date as the spouse's benefit.
- 3.08. Effective as of March 1, 2004, all rights and / or obligations of the Company to honor single-sum withdrawal requests shall be terminated.

- 3.09. Effective January 1, 2005, notwithstanding any provision of this Plan to the contrary, if the Member is considered a Specified Employee at termination of employment under such procedures as established by the Company in accordance with Section 409A of the Internal Revenue Code, benefit distributions that are made by reason of termination of employment may not commence earlier than six (6) months after the date of such termination of employment. Therefore, in the event this Section 3.09 is applicable to a Member, any distribution that would otherwise be paid to the Member within the first six months following the termination of employment shall be accumulated and paid to the Participant in a lump sum (payable with interest determined based upon the short-term applicable federal rate (AFR) for purposes of Section 1274(d) of the Internal Revenue Code for the November preceding the calendar year of the termination of employment) on the first day of the seventh month following the termination of employment. All subsequent distributions shall be paid in the manner specified.
- 3.10. Notwithstanding any other provision of the Plan to the contrary, a Member may request at any time to receive a lump sum distribution of a portion of his supplemental benefit due to an "Unforeseeable Emergency" as follows:
- (a) "Unforeseeable Emergency" shall mean any severe financial hardship to the Member resulting from an illness or accident of the Member or his spouse or dependent (as defined in Section 152 of the Internal Revenue Code, without regard to Sections 152(b)(1), (b)(2) and (d)(1)(B) thereof), loss of the Member's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the Member.
  - (b) Any distribution pursuant to this provision is limited to the amount necessary to meet the emergency, and any amounts necessary to pay any federal, state, local or foreign income taxes or penalties reasonably anticipated to result from such distribution.
  - (c) The circumstances that will constitute an Unforeseeable Emergency will depend upon the facts of each case, but, in any case, payment may not be made to the extent that such hardship is or may be relieved (i) through reimbursement or compensation by insurance or otherwise or (ii) by liquidation of the Participant's assets, to the extent the liquidation of such assets would not itself cause severe financial hardship.
  - (d) If the Committee determines that a Participant has demonstrated an Unforeseeable Emergency, the determination to make a distribution pursuant to this Section 3.10 remains in the sole discretion of the Committee.
  - (e) Any distribution due to an Unforeseeable Emergency shall be made by determining the Actuarial Equivalent Present Value of the Member's supplemental benefits and a lump sum distribution shall not be in excess of such Actuarial Equivalent Present Value. In the event the distribution is less than the Actuarial Equivalent Present Value, the Actuarial Equivalent Present value of the Member's supplemental benefits shall then be reduced in accordance with Section 3.01(d).

#### Article 4. Administration

- 4.01. The administration of the Plan and the responsibility for carrying out its provisions are vested in a Retirement Committee which shall be composed of the members of the Retirement Committee provided for under Article IX of the Retirement Income Plan. The provisions of Article IX of the Retirement Income Plan concerning powers of the Committee shall apply under this Plan. The Retirement Committee shall have the full and exclusive discretion and authority to interpret the Plan and to determine all benefits and to resolve all questions arising from the administration, interpretation, and application of Plan provisions, either by general rules or by particular decisions, including determinations as to whether a claimant is eligible for benefits, the amount, form and timing of benefits, and any other matter (including any question of fact) raised by a claimant or identified by the Retirement Committee. All decisions of the Committee shall be conclusive and binding upon all affected persons. The expenses of the Committee shall be paid directly by the Company.

#### Article 5. General Provisions

- 5.01. The establishment of the Plan shall not be construed as conferring any legal rights upon any person for a continuation of employment, nor shall it interfere with the rights of the Company to discharge any employee and to treat him without regard to the effect which such treatment might have upon him as a Member of the Plan. No legal or beneficial interest in any of the Company's assets is intended to be conferred by the terms of the Plan.
- 5.02. In the event that the Committee shall find that a Member or other person entitled to benefits hereunder is unable to care for his affairs because of illness or accident, the Committee may direct that any benefit payment due him, unless claim shall have been made therefor by a duly appointed legal representative, be paid to his spouse, a child, a parent or other blood relative, or to a person with whom he resides, and any such payment so made shall be a complete discharge of the liabilities of the Company and the Plan therefor.
- 5.03. The Company shall have the right to deduct from each payment to be made under the Plan any required withholding taxes.
- 5.04. Subject to any applicable law, no benefit under the Plan shall be subject in any manner to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance or charge, any attempt so to do shall be void, nor shall any such benefit be in any manner liable for or subject to garnishment, attachment, execution or levy, or liable for or subject to the debts, contracts, liabilities, engagements or torts of the Member. In the event that the Committee shall find that any Member or other person entitled to benefits hereunder has become bankrupt or has made any such attempt with respect to any such benefit, such benefit shall cease and terminate, and in that event the Board shall hold or apply the same to or for the benefit of such Member or other person entitled to benefits.

- 5.05. (a) In the event that a Member (i) is discharged for willful, deliberate, or gross misconduct as determined by the Board of Directors or a duly constituted committee thereof; or (ii) if following the Member's termination of employment with the Company and, within a period of three years thereafter, the Member engages in any business or enters into any employment which the Board of Directors or a duly constituted committee thereof determines to be either directly or indirectly competitive with the business of the Company or substantially injurious to the Company's financial interest (the occurrence of an event described in (i) or (ii) shall be referred to as "Injurious Conduct"), all benefits which would otherwise be payable to him under the Plan shall be forfeited. Further, the Board of Directors or a duly constituted committee thereof, in its discretion, may require the Member who has engaged in Injurious Conduct to return any amounts previously received by the Member, provided the right to require repayment under this subsection (a) must be exercised within ninety (90) days after the Board (or committee, as the case may be) first learns of the Injurious Conduct, but in no event later than twenty-four (24) months after the Member's termination of employment with the Company. A Member may request the Board of Directors or a duly constituted committee thereof, in writing, to determine whether any proposed business or employment activity would constitute Injurious Conduct. Such a request shall fully describe the proposed activity and the Board's (or the committee's, as the case may be) determination shall be limited to the specific activity so described.
- (b) Notwithstanding the foregoing, benefits shall not cease or be forfeited or be required to be repaid merely because the Member (1) owns publicly traded shares of stock of a corporation which competes with the Company, or (2) (a) acts as a consultant for, (b) has an investment in, or (c) is a Board member of a business where after the Member notifies the Company in writing in advance of his potential involvement under (2)(a), (b) or (c), the Company's Board of Directors or a duly constituted committee thereof determines that the Member will not be in violation of the Company's Conflicts of Interest policy, or (3) becomes associated with a business which competes with the Company within two years following a "Change in Control" and is eligible for benefits under any individual severance agreement.
- 5.06. The Plan shall be constructed, regulated and administered under the laws of the Commonwealth of Pennsylvania.
- 5.07. The masculine pronoun shall mean the feminine wherever appropriate.

- 5.08. The Board of Directors may, through written resolutions adopted by the Board of Directors, amend or discontinue the Retirement Benefit Equity Plan at any time; provided, however, that if the Plan is amended to discontinue or reduce the amount of supplemental benefit payments (except as may be required pursuant to any plan arising from insolvency or bankruptcy proceedings) (a) any Member who is being paid his supplemental benefits immediately prior to the effective date of the amendment shall continue to be paid his supplemental benefits in the amount and manner (as provided under Article 3 hereof) as they were being paid at the time of such amendment, and (b) any Member who is not being paid his supplemental benefits immediately prior to the effective date of the amendment shall be entitled to receive (i) the supplemental benefits accrued by such Member as of the effective date of the amendment, with such supplemental benefits being paid at the time elected by the Member under Section 3.02, and (ii) any legal fees and related expenses incurred by the Member in receiving such supplemental benefits (as permitted under Section 5.09(e)) and interest under Section 5.09(f) (to the extent applicable). Notwithstanding the preceding sentence, any written employment agreement between the Executive Committee and any Member described in clause (b) of the preceding sentence shall govern to the extent such agreement either amends or discontinues the Member's supplemental benefits under the Plan, and Section 5.05 shall govern to the extent any Member engages in Injurious Conduct as defined under that section.
- 5.09. (a) Any person claiming a benefit, requesting an interpretation or ruling under the Plan, or requesting information under the Plan shall present the request in writing to the Committee which shall respond in writing as soon as practicable.
- (b) If the claim or request is denied, the written notice of denial shall state:
- (i) The reasons for denial, with specific reference to the Plan provisions on which the denial is based.
  - (ii) A description of any additional material or information required and an explanation of why it is necessary.
  - (iii) An explanation of the Plan's claim review procedure.
- (c) Any person whose claim or request is denied or who has not received a response within thirty (30) days may request review by notice given in writing to the Committee. The claim or request shall be reviewed by the Committee who may, but shall not be required to, grant the claimant a hearing. On review, the claimant may have representation, examine pertinent documents, and submit issues and comments in writing.

- (d) The decision on review shall normally be made within sixty (60) days. If an extension of time is required for a hearing or other special circumstances, the claimant shall be notified and the time limit shall be one hundred twenty (120) days. The decision shall be in writing and shall state the reasons and the relevant Plan provisions. All decisions on review shall be final and bind all parties concerned.
- (e) In the event a Member's claim for supplemental benefits under this Plan is denied and the Member successfully appeals the denial of such claim under the foregoing procedures, the Company shall pay or reimburse the legal fees and expenses directly incurred by the Member in connection with his appeal subject to a maximum payment or reimbursement of one-third of the Actuarial Equivalent Present Value of the supplemental benefits to which the Member is entitled. For purposes of the preceding sentence, actuarial equivalence shall be determined using the actuarial assumptions and factors reasonably utilized under the Retirement Income Plan as of the date of determination. Any such legal fees and expenses shall be paid by the Company to, or on behalf of, the Member no later than thirty (30) days following the Member's written request for the payment of such legal fees and expenses, provided the Member supplies the Committee with evidence of the fees and expenses incurred by the Member that the Committee, in its sole discretion, determines is sufficient.
- (f) Further, in the event a Member's claim for supplemental benefits under this Plan is denied and the Member successfully appeals the denial of such claim under the foregoing procedures, the Company shall pay to the Member interest on the portion of the Member's supplemental benefits that were not otherwise paid when due because of the initial denial of the claim. For purposes of the preceding sentence, interest shall accrue at an annual rate equal to the prime rate as quoted in the Wall Street Journal as of the date the supplemental benefits would otherwise have been paid if the claim had not initially been denied, plus five percent (5%), and shall be adjusted as necessary to reflect any partial payment or payments of the amounts owed to the Member.

**ARMSTRONG WORLD INDUSTRIES, INC.**  
**2006 LONG-TERM INCENTIVE PLAN**  
**EFFECTIVE AS OF October 2, 2006**

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**ARMSTRONG WORLD INDUSTRIES, INC.**

**2006 LONG-TERM INCENTIVE PLAN**

1. **Purpose.** Armstrong World Industries, Inc. 2006 Long-Term Incentive Plan (the “Plan”) is intended to provide incentives which will attract, retain and motivate highly competent persons as officers and key employees of Armstrong World Industries, Inc., a Pennsylvania corporation (the “Company”), and its subsidiaries and affiliates, by providing them with appropriate incentives and rewards to encourage them to enter into and continue in the employ of the Company, to acquire a proprietary interest in the long-term success of the Company and to reward the performance of individuals in fulfilling their personal responsibilities for long-range achievements.

**2. Administration.**

(a) Committee. The Plan will be administered by a committee (the “Committee”) appointed by the Board of Directors of the Company from among its members (which may be the Management Development and Compensation Committee) and shall be comprised, unless otherwise determined by the Company’s Board of Directors, solely of not less than two (2) members who shall be (i) “Non-Employee Directors” within the meaning of Rule 16b-3(b)(3) (or any successor rule) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) and (ii) “outside directors” within the meaning of Treasury Regulation Section 1.162-27(e)(3) under Section 162(m) of the Internal Revenue Code of 1986, as amended (the “Code”).

(b) Authority. The Committee is authorized, subject to the provisions of the Plan, to establish such rules and regulations as it deems necessary for the proper administration of the Plan and to make such determinations and interpretations and to take such action in connection with the Plan and any Benefits granted hereunder as it deems necessary or advisable. All determinations and interpretations made by the Committee shall be binding and conclusive on all participants and their legal representatives.

(c) Indemnification. No member of the Committee and no employee of the Company shall be liable for any act or failure to act hereunder, except in circumstances involving his or her bad faith or willful misconduct, or for any act or failure to act hereunder by any other member or employee or by any agent to whom duties in connection with the administration of this Plan have been delegated. The Company shall indemnify members of the Committee and any agent of the Committee who is an employee of the Company, a subsidiary or an affiliate against any and all liabilities or expenses to which they may be subjected by reason of any act or failure to act with respect to their duties on behalf of the Plan, except in circumstances involving such person’s bad faith or willful misconduct.



(d) Delegation and Advisers . The Committee may delegate to one or more of its members, to management or to one or more agents, such administrative duties as it may deem advisable; provided, such delegation does not adversely effect the exemption provided by Rule 16b-3 of the Exchange Act, prevent a Benefit from qualifying as a Performance-Based Award, if so intended, and complies with applicable law. The Committee, or any person to whom it has delegated duties as aforesaid, may employ one or more persons to render advice with respect to any responsibility the Committee or such person may have under the Plan. The Committee may employ such legal or other counsel, consultants and agents as it may deem desirable for the administration of the Plan and may rely upon any opinion or computation received from any such counsel, consultant or agent. Expenses incurred by the Committee in the engagement of such counsel, consultant or agent shall be paid by the Company, or the subsidiary or affiliate whose employees have benefited from the Plan, as determined by the Committee.

3. **Participants** . Participants will consist of such officers and key employees of the Company and its subsidiaries and affiliates as the Committee in its sole discretion determines to be significantly responsible for the success and future growth and profitability of the Company and whom the Committee may designate from time to time to receive Benefits under the Plan. Designation of a participant in any year shall not require the Committee to designate such person to receive a Benefit in any other year or, once designated, to receive the same type or amount of Benefit as granted to the participant in any other year. The Committee shall consider such factors as it deems pertinent in selecting participants and in determining the type and amount of their respective Benefits.

4. **Type of Benefits** . Benefits under the Plan may be granted in any one or a combination of (a) Stock Options, (b) Stock Appreciation Rights, (c) Restricted Stock Awards, (d) Stock Units and (e) Cash Awards (each as described below, and collectively, the “Benefits”). Restricted Stock Awards, Stock Units and Cash Awards may, as determined by the Committee in its discretion, constitute Performance-Based Awards, as described in Section 11 hereof. Benefits granted under the Plan may be evidenced by an agreement (which need not be identical) that may provide additional terms and conditions associated with such Benefits, as determined by the Committee in its sole discretion, *provided, however*, that in the event of any conflict between the provisions of the Plan and any such agreement, the provisions of the Plan shall prevail.

#### 5. **Common Stock Available Under the Plan.**

(a) Basic Limitations . The aggregate number of shares of common stock of the Company (the “Common Stock”) that may be subject to Benefits, granted under this Plan shall be 5,349,000 shares of Common Stock, which may be authorized and unissued shares or treasury shares or may be purchased on the open market or by private purchase, subject to any adjustments made in accordance with Section 14(a) hereof. The maximum number of shares of Common Stock with respect to which Benefits may be granted or measured to any individual participant under the Plan in any one calendar year shall not exceed 750,000 (subject to adjustments made in accordance with Section 14(a) hereof).

(b) Additional Shares. Any shares of Common Stock subject to (or referenced by) a Benefit which are not ultimately used to settle a Benefit shall again be available for Benefits under this Plan and any shares of Common Stock delivered to the Company as part or full payment for the exercise of a Stock Option, Stock Appreciation Right, or Restricted Stock Award or to satisfy a tax obligation shall also be available for Benefits under this Plan. This includes shares of Common Stock that are: (i) covered by a Stock Option or referenced by a Stock Appreciation Right which for any reason is cancelled or terminated without having been exercised, (ii) subject to Restricted Stock Awards or Stock Units which are forfeited, and (iii) not delivered to a participant because all or a portion of a Benefit is settled in cash. The preceding sentences of this Section shall apply only for purposes of determining the aggregate number of shares of Common Stock subject to Benefits but shall not apply for purposes of determining the maximum number of shares of Common Stock with respect to which Benefits (including the maximum number of shares of Common Stock subject to Stock Options and Stock Appreciation Rights) that may be granted to any individual participant under the Plan.

(c) Acquisitions. In connection with the acquisition of any business by the Company or any of its subsidiaries or affiliates, any outstanding grants, awards or sales of options or other similar rights pertaining to such business may be assumed or replaced by Benefits under the Plan upon such terms and conditions as the Committee determines in its sole discretion.

## **6. Stock Options.**

(a) Generally. Stock Options will consist of awards from the Company that will enable the holder to purchase a number of shares of Common Stock, at set terms. Stock Options may be “incentive stock options” (“Incentive Stock Options”), within the meaning of Section 422 of the Code, or Stock Options which do not constitute Incentive Stock Options (“Nonqualified Stock Options”). The Committee will have the authority to grant to any participant one or more Incentive Stock Options, Nonqualified Stock Options, or both types of Stock Options (in each case with or without Stock Appreciation Rights). Each Stock Option shall be subject to such terms and conditions, including vesting, consistent with the Plan as the Committee may impose from time to time, subject to the following limitations.

(b) Exercise Price. Each Nonqualified Stock Option granted hereunder shall have a per-share exercise price as the Committee may determine on the date of grant.

(c) Payment of Exercise Price. The option exercise price may be paid in cash or, in the discretion of the Committee, by the delivery of shares of Common Stock of the Company then owned by the participant, provided such shares have been held by such participant for at least six (6) months. In the discretion of the Committee, payment may also be made by delivering a properly executed exercise notice to the Company together with a copy of irrevocable instructions to a broker to deliver promptly to the Company the amount of sale or loan proceeds to pay the exercise price as long as such transaction does not constitute an impermissible loan to an executive officer under the Sarbanes-Oxley Act of 2002. To facilitate the foregoing, the Company may enter into agreements for coordinated procedures with one or more brokerage firms. The Committee may prescribe any other method of paying the exercise price that it determines to be consistent with applicable law and the purpose of the Plan, including, without limitation, in lieu of the exercise of a Stock Option by delivery of shares of Common Stock of the Company then owned by a participant, providing the Company with a notarized statement attesting to the number of shares owned, where upon verification by the Company, the Company would issue to the participant only the number of incremental shares to which the participant is entitled upon exercise of the Stock Option.

(d) Exercise Period . Stock Options granted under the Plan shall be exercisable at such time or times and subject to such terms and conditions, including vesting, as shall be determined by the Committee; *provided, however* , that no Stock Option shall be exercisable later than ten (10) years after the date it is granted. All Stock Options shall terminate at such earlier times and upon such conditions or circumstances as the Committee shall in its discretion set forth in such option agreement on the date of grant.

(e) Restoration of Stock Options . The Committee may, at the time of grant of an option, provide for the grant of a subsequent Restoration Stock Option if the exercise price is paid for by delivering previously owned shares of Common Stock of the Company. Restoration Stock Options (i) may be granted in respect of no more than the number of shares of Common Stock tendered in exercising the predecessor Stock Option, (ii) shall have an exercise price equal to the Fair Market Value (as defined in Section 17 below) on the date the Restoration Stock Option is granted, and (iii) may have an exercise period that does not extend beyond the remaining term of the predecessor Stock Option. In determining which methods a participant may utilize to pay the exercise price, the Committee may consider such factors as it determines are appropriate.

(f) Limitations on Incentive Stock Options . Incentive Stock Options may be granted only to participants who are employees of the Company or of a “Parent Corporation” or “Subsidiary Corporation” (as defined in Sections 424(e) and (f) of the Code, respectively) on the date of grant. The aggregate Fair Market Value (determined as of the time the Stock Option is granted) of the Common Stock with respect to which Incentive Stock Options are exercisable for the first time by a participant during any calendar year (under all option plans of the Company and of any Parent Corporation or Subsidiary Corporation) shall not exceed one hundred thousand dollars (\$100,000), provided, however, that if such \$100,000 limit is exceeded, the excess Incentive Stock Options shall be treated as Nonqualified Stock Options. For purposes of the preceding sentence, Incentive Stock Options will be taken into account in the order in which they are granted. The per-share exercise price of an Incentive Stock Option shall not be less than one hundred percent (100%) of the Fair Market Value of the Common Stock on the date of grant, and no Incentive Stock Option may be exercised later than ten (10) years after the date it is granted.

(g) Additional Limitations on Incentive Stock Options for Ten Percent Shareholders . Incentive Stock Options may not be granted to any participant who, at the time of grant, owns stock possessing (after the application of the attribution rules of Section 424(d) of the Code) more than ten percent (10%) of the total combined voting power of all classes of stock of the Company or any Parent Corporation or Subsidiary Corporation, unless the exercise price of the option is fixed at not less than one hundred ten percent (110%) of the Fair Market Value of the Common Stock on the date of grant and the exercise of such option is prohibited by its terms after the expiration of five (5) years from the date of grant of such option.

## 7. Stock Appreciation Rights.

(a) Generally. The Committee may, in its discretion, grant Stock Appreciation Rights, including a concurrent grant of Stock Appreciation Rights in tandem with any Stock Option grant. A Stock Appreciation Right means a right to receive a payment in cash, Common Stock or a combination thereof, as determined by the Committee, in an amount equal to the excess of (i) the Fair Market Value, or other specified valuation, of a specified number of shares of Common Stock on the date the right is exercised over (ii) the Fair Market Value of such shares of Common Stock on the date the right is granted, or other specified amount, all as determined by the Committee; *provided, however*, that if a Stock Appreciation Right is granted in tandem with or in substitution for a Stock Option, the designated Fair Market Value in the award agreement shall reflect the Fair Market Value on the date such Stock Option was granted. Each Stock Appreciation Right shall be subject to such terms and conditions, including vesting, as the Committee shall impose from time to time, provided, however, that if a Stock Appreciation Right is granted in connection with a Stock Option, the Stock Appreciation Right shall become exercisable, be transferable and shall expire according to the same vesting, transferability and expiration rules as the corresponding Stock Option.

(b) Exercise Period. Stock Appreciation Rights granted under the Plan shall be exercisable at such time or times and subject to such terms and conditions, including vesting, as shall be determined by the Committee; *provided, however*, that no Stock Appreciation Rights shall be exercisable later than ten (10) years after the date it is granted. All Stock Appreciation Rights shall terminate at such earlier times and upon such conditions or circumstances as the Committee shall in its discretion set forth in such right at the date of grant.

## 8. Restricted Stock Awards.

(a) Generally. The Committee may, in its discretion, grant Restricted Stock Awards consisting of Common Stock issued or transferred to participants with or without other payments therefor.

(b) Payment of the Purchase Price. If the Restricted Stock Award requires payment therefor, the purchase price of any shares of Common Stock subject to a Restricted Stock Award may be paid in any manner authorized by the Committee, which may include any manner authorized under the Plan for the payment of the exercise price of a Stock Option. Restricted Stock Awards may also be made in consideration of services rendered to the Company or its subsidiaries or affiliates.

(c) Additional Terms. Restricted Stock Awards may be subject to such terms and conditions, including vesting, as the Committee determines appropriate, including, without limitation, (i) restrictions on the sale or other disposition of such shares, and (ii) the right of the Company to reacquire such shares for no consideration upon termination of the participant's employment within specified periods, the participant's competition with the Company, or the participant's breach of other obligations to the Company. Restricted Stock Awards may constitute Performance-Based Awards, as described in Section 11 hereof. The Committee may require the participant to deliver a duly signed stock power, endorsed in blank, relating to the Common Stock covered by such an Award. The Committee may also require that the stock certificates evidencing such shares be held in custody or bear restrictive legends until the restrictions thereon shall have lapsed.

(d) Rights as a Shareholder. The participant shall have, with respect to the shares of Common Stock subject to a Restricted Stock Award, all of the rights of a holder of shares of Common Stock of the Company, including the right to vote the shares. At the discretion of the Committee, cash dividends and stock dividends with respect to the Restricted Stock may be either currently paid to the participant or withheld by the Company for the participant's account, and interest may be credited on the amount of cash dividends withheld at a rate and subject to such terms as determined by the Committee. The cash dividends or stock dividends so withheld by the Committee and attributable to any particular share of Restricted Stock (and earnings thereon, if applicable) shall be distributed to the participant upon the release of restrictions on such shares and, if such share is forfeited, the participant shall have no right to such cash dividends or stock dividends.

#### **9. Stock Units.**

(a) Generally. The Committee may, in its discretion, grant Stock Units (as defined in subsection (c) below) to participants hereunder. Stock Units may be subject to such terms and conditions, including vesting, as the Committee determines appropriate. Stock Units may constitute Performance-Based Awards, as described in Section 11 hereof. A Stock Unit granted by the Committee shall provide payment in shares of Common Stock at such time as the award agreement shall specify. Shares of Common Stock issued pursuant to this Section 9 may be issued with or without other payments therefor as may be required by applicable law or such other consideration as may be determined by the Committee. The Committee shall determine whether a participant granted a Stock Unit shall be entitled to a Dividend Equivalent Right (as defined in subsection (c) below).

(b) Settlement of Stock Units. Shares of Common Stock representing the Stock Units shall be distributed to the participant unless the Committee provides for the payment of the Stock Units in cash equal to the value of the shares of Common Stock which would otherwise be distributed to the participant or partly in cash and partly in shares of Common Stock.

(c) Definitions. A “Stock Unit” means a notional account representing one (1) share of Common Stock. A “Dividend Equivalent Right” means the right to receive the amount of any dividend paid on the share of Common Stock underlying a Stock Unit, which shall be payable in cash or in the form of additional Stock Units.

**10. Cash Awards.** The Committee may, in its discretion, grant awards to be settled solely in cash (“Cash Awards”). Cash Awards may be subject to such terms and conditions, including vesting, as the Committee determines appropriate. Cash Awards may constitute Performance-Based Awards, as described in Section 11 hereof. The maximum Cash Award payout that may be made to any participant in any one year is \$3,000,000.

## 11. Performance-Based Awards.

(a) Generally. Any Benefits granted under the Plan may be granted in a manner such that the Benefits qualify for the performance-based compensation exemption of Section 162(m) of the Code (“Performance-Based Awards”). As determined by the Committee in its sole discretion, either the granting or vesting of such Performance-Based Awards shall be based on achievement of performance objectives that are based on one or more of the business criteria described below that apply to the individual participant, one or more business units or the Company as a whole.

(b) Business Criteria. The business criteria shall be as follows, individually or in combination: (i) net earnings; (ii) earnings per share; (iii) sales; (iv) operating income; (v) earnings before interest and taxes (EBIT); (vi) earnings before interest, taxes, depreciation and amortization (EBITDA); (vii) cash flow; (viii) working capital targets; (ix) return on equity; (x) return on capital; (xi) market price per share; and (xii) total return to shareholders. In addition, Performance-Based Awards may include comparisons to the performance of other companies, such performance to be measured by one or more of the foregoing business criteria.

(c) Establishment of Performance Goals. With respect to Performance-Based Awards, the Committee shall establish in writing (i) the performance goals applicable to a given period, and such performance goals shall state, in terms of an objective formula or standard, the method for computing the amount of compensation payable to the participant if such performance goals are obtained and (ii) the individual employees or class of employees to which such performance goals apply; provided, however, that such performance goals shall be established in writing no later than ninety (90) days after the commencement of the applicable performance period (but in no event after twenty-five percent (25%) of such performance period has elapsed).

(d) Certification of Performance. No Performance-Based Awards shall be payable to or vest with respect to, as the case may be, any participant for a given period until the Committee certifies in writing that the objective performance goals (and any other material terms) applicable to such period have been satisfied.

(e) Modification of Performance-Based Awards. With respect to any Benefits intended to qualify as Performance-Based Awards, after establishment of a performance goal, the Committee shall not revise such performance goal or increase the amount of compensation payable thereunder (as determined in accordance with Section 162(m) of the Code) upon the attainment of such performance goal. Notwithstanding the preceding sentence, the Committee may reduce or eliminate the number of shares of Common Stock or cash granted or the number of shares of Common Stock vested upon the attainment of such performance goal.

12. **Foreign Laws.** The Committee may grant Benefits to individual participants who are subject to the tax laws of nations other than the United States, which Benefits may have terms and conditions as determined by the Committee as necessary to comply with applicable foreign laws. The Committee may take any action which it deems advisable to obtain approval of such Benefits by the appropriate foreign governmental entity; *provided, however*, that no such Benefits may be granted pursuant to this Section 12 and no action may be taken which would result in a violation of the Exchange Act, the Code or any other applicable law.

### 13. Certain Terminations of Employment; Forfeitures.

(a) Forfeiture of Unsettled Benefits. Unless the Committee or any agreement providing for Benefits under this Plan shall otherwise provide, a participant shall forfeit all Benefits, which have not been settled under this Plan (other than fully vested Restricted Stock Awards) if:

(i) the participant's employment with the Company or with any Parent Corporation or Subsidiary Corporation is terminated for willful, deliberate, or gross misconduct, as determined by the Committee, in its sole discretion, or

(ii) following the participant's termination of employment with the Company (or with any Parent Corporation or Subsidiary Corporation) and for a period of two (2) years thereafter, the participant engages in any business or enters into any employment relationship which the Committee in its sole discretion determines to be either directly or indirectly competitive with the business of the Company or substantially injurious to the Company's business interest.

The activities described in (i) and (ii) above are hereafter referred to as "Injurious Conduct".

(b) Forfeiture of Settled Benefits. If the Committee determines that a participant has engaged in Injurious Conduct during the course of his employment (or during the two (2) year period following his or her termination of employment), the Committee may in its discretion require the participant to return to the Company any Common Stock or cash received in settlement of any Benefit under this Plan. If the Common Stock acquired in settlement of a Benefit has been disposed of by the participant, then the Company may require the participant to pay to the Company the economic value of the Common Stock as of the date of disposition.

(c) Timing. The Committee shall exercise the right of forfeiture provided to the Company in this Section 13 within ninety (90) days after the discovery of the activities giving rise to the Company's right of forfeiture, which activities must have occurred no later than twenty-four (24) months after the participant's termination of employment.

(d) Determination from the Committee. A participant may make a request to the Committee in writing for a determination regarding whether any proposed business or activity would constitute Injurious Conduct. Such request shall fully describe the proposed business or activity. The Committee shall respond to the participant in writing and the Committee's determination shall be limited to the specific business or activity so described.

(e) Condition Precedent. Unless the Committee or any agreement providing for Benefits under this Plan shall otherwise provide, no Benefit shall be deemed awarded to any participant under this Plan unless and until the participant agrees to the applicability of this Section 13.

(f) Enforceability. The purpose of this Section 13 is to protect the Company (and any Parent and Subsidiaries) from Injurious Conduct. To the extent that this Section 13 is not fully enforceable as written, the unenforceable provisions shall be modified so as to provide the Company with the fullest protection permitted by law.

#### 14. Adjustment Provisions; Change in Control.

(a) Adjustment. Benefits granted under the Plan and any agreements evidencing such Benefits, the maximum number of shares of Common Stock subject to all Benefits stated in Section 5(a) and the maximum number of shares of Common Stock with respect to which Benefits may be granted to any one person during any period stated in Section 5(a) shall be subject to mandatory adjustment or substitution, as determined by the Committee in its sole discretion, as to the number, price or kind of a share of Common Stock or other consideration subject to such Benefits or as otherwise determined by the Committee to be equitable (i) in the event of changes in the outstanding Common Stock or in the capital structure of the Company by reason of stock or extraordinary cash dividends, stock splits, reverse stock splits, recapitalization, reorganizations, mergers, consolidations, combinations, exchanges, or other relevant changes in capitalization occurring after the date of grant of any such Benefit or (ii) in the event of any change in applicable laws or any change in circumstances which results in or would result in any substantial dilution or enlargement of the rights granted to, or available for, participants, or which otherwise warrants equitable adjustment because it interferes with the intended operation of the Plan. Any adjustment in Incentive Stock Options under this Section 14 shall be made only to the extent not constituting a “modification” within the meaning of Section 424(h)(3) of the Code, and any adjustments under this Section 14 shall be made in a manner which does not adversely affect the exemption provided pursuant to Rule 16b-3 under the Exchange Act. Further, with respect to Benefits intended to qualify as “performance-based compensation” under Section 162(m) of the Code, such adjustments or substitutions shall be made only to the extent that the Committee determines that such adjustments or substitutions may be made without causing the Company to be denied a tax deduction on account of Section 162(m) of the Code. The Company shall give each participant notice of an adjustment hereunder and, upon notice, such adjustment shall be conclusive and binding for all purposes.

(b) Effect of a Change in Control. Notwithstanding any other provision of this Plan, if there is a Change in Control (as defined in subsection (c) below) of the Company, all then outstanding Stock Options, Stock Appreciation Rights and Stock Units shall immediately vest and become exercisable and any restrictions on Restricted Stock Awards or Stock Units shall immediately lapse. Thereafter, insofar as any Benefit is provided in shares of stock of the Company or in Stock Options or Stock Appreciation Rights or is determined based on the value or other attributes of a share of stock of the Company, such Benefit shall be subject to the same terms to which a share of stock of the Company is subject in accordance with any agreement effecting the Change in Control, which agreement, may provide, without limitation, that each Stock Option and Stock Appreciation Right outstanding hereunder shall terminate within a specified number of days after notice to the holder, and that such holder shall receive, with respect to each share of Common Stock subject to such Stock Option or Stock Appreciation Right, an amount equal to the excess of the Fair Market Value of such shares of Common Stock immediately prior to the occurrence of such Change in Control over the exercise price per share underlying such Stock Option or Stock Appreciation Right with such amount payable in cash, in one or more kinds of property (including the property, if any, payable in the transaction) or in a combination thereof, as the Committee, in its discretion, shall determine.



(c) Definitions. For purposes of this Section 14, the following words shall have the meaning ascribed to them below:

(i) “ Affiliate ” means (i) any entity that directly or indirectly is controlled by, controls or is under common control with the Company and (ii) any entity in which the Company has a significant equity interest, in either case as determined by the Committee.

(ii) “ Beneficial Owner ” shall have the meaning set forth in Rule 13d-3 under the Exchange Act.

(iii) “ Change in Control ” of the Company, with respect to any participant, shall be deemed to have occurred upon any of the following events (unless another definition is provided in any applicable individual change in control agreement between the Company and the participant, in which case such agreement shall govern):

(A) Any Person becomes the Beneficial Owner, directly or indirectly, of securities of the Company (not including in the securities beneficially owned by such Person any securities acquired directly from the Company or its affiliates) representing twenty percent (20%) or more of either the then outstanding shares of Common Stock or the combined voting power of the Company’s then outstanding securities, excluding any Person who becomes such a Beneficial Owner in connection with a transaction described in clause (i) of Paragraph (C) below;

(B) The following individuals cease for any reason to constitute a majority of the number of directors then serving: individuals who, on the Effective Date (as defined in Section 24 below), constitute the Board of Directors and any new director (other than a director whose initial assumption of office is in connection with an actual or threatened election contest, including but not limited to a consent solicitation, relating to the election of directors of the Company) whose appointment or election by the Board of Directors or nomination for election by the Company’s shareholder’s was approved by a vote of least two-thirds (2/3) of the directors then still in office who either were directors on the Effective Date or whose appointment, election or nomination for election was previously so approved; or

(C) There is consummated a merger or consolidation of the Company (including a triangular merger to which the Company is a party) with any other corporation other than (i) a merger or consolidation which would result in the voting securities of the Company outstanding immediately prior to such merger or consolidation continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity or any parent thereof) at least sixty-six and two-thirds percent (66-2/3%) of the combined voting power of the voting securities of the Company or such surviving entity outstanding immediately after such merger or consolidation; or (ii) a merger or consolidation effected to implement a recapitalization of the Company (or similar transaction in which no Person is or becomes the Beneficial Owner, directly or indirectly, of securities of the Company (not including in the securities beneficially owned by such Person any securities acquired directly from the Company or its subsidiaries) representing twenty percent (20%) or more of either the then outstanding shares of Common Stock or the combined voting power of the Company’s then outstanding securities;

(D) The shareholders of the Company approve a plan of complete liquidation or dissolution of the Company or there is consummated an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets, other than a sale or disposition by the Company of all or substantially all of the Company's assets to an entity at least seventy-five percent (75%) of the combined voting power of the voting securities of which are owned by shareholders of the Company in substantially the same proportions as their ownership of the Company immediately prior to such sale. Notwithstanding the foregoing, no "Change in Control" shall be deemed to have occurred if there is consummated any transaction or series of integrated transactions immediately following which the record holders of the Common Stock immediately prior to such transaction or series of transactions continue to have substantially the same proportionate ownership in the entity which owns all or substantially all of the assets of the Company immediately following such transaction or series of transactions.

(iv) "Person" shall have the meaning given in Section 3(a)(9) of the Exchange Act, as modified and used in Section 13(d) and 14(d) thereof, except that such term shall not include (A) the Company or any of its subsidiaries, (B) a trustee or other fiduciary holding securities under an employee benefit plan of the Company or any of its subsidiaries, (C) an underwriter temporarily holding securities pursuant to an offering of such securities, (D) a corporation owned, directly or indirectly, by the shareholders of the Company in substantially the same proportion as their ownership of the Common Stock, or (E) an entity or entities which are eligible to file and have filed a Schedule 13G under Rule 13d-1(b) under the Exchange Act, which Schedule indicates beneficial ownership of fifteen percent (15%) or more of the outstanding shares of Common Stock or of the combined voting power of the Company's then outstanding securities.

15. **Nontransferability.** Each Benefit granted under the Plan to a participant (other than awards of unrestricted Stock Awards, vested restricted Stock Awards and vested Cash Awards) shall not be transferable otherwise than by will or the laws of descent and distribution, and shall be exercisable, during the participant's lifetime, only by the participant. In the event of the death of a participant, each Stock Option or Stock Appreciation Right theretofore granted to him or her shall be exercisable during such period after his or her death as the Committee shall in its discretion set forth in such option or right at the date of grant and then only by the executor or administrator of the estate of the deceased participant or the person or persons to whom the deceased participant's rights under the Stock Option or Stock Appreciation Right shall pass by will or the laws of descent and distribution. Notwithstanding the foregoing, at the discretion of the Committee, an award of a Benefit other than an Incentive Stock Option may permit the transferability of a Benefit by a participant solely to the participant's spouse, siblings, parents, children and grandchildren or trusts for the benefit of such persons or partnerships, corporations, limited liability companies or other entities owned solely by such persons, including trusts for such persons, subject to any restriction included in the award of the Benefit.

16. **Other Provisions.** The award of any Benefit under the Plan may also be subject to such other provisions (whether or not applicable to the Benefit awarded to any other participant) as the Committee determines appropriate, including, without limitation, for the forfeiture of, or restrictions on resale or other disposition of, Common Stock acquired under any form of Benefit, for the acceleration of exercisability or vesting of Benefits, or to comply with federal and state securities laws, or understandings or conditions as to the participant's employment in addition to those specifically provided for under the Plan.

17. **Fair Market Value.** For purposes of this Plan and any Benefits awarded hereunder, Fair Market Value on any given date means (i) if the Common Stock is listed on a national securities exchange or is quoted in the National Market System of the National Association of Securities Dealers Automated Quotation System ("NASDAQ") on a last sale basis, the closing price reported as having occurred on the such date, or, if there is no sale on such date, then on the last preceding date on which such a sale was reported, or (ii) if the Common Stock is not listed on a national securities exchange nor quoted in NASDAQ on a last sale basis, the amount determined by the Committee to be the fair market value based upon a good faith attempt to value the Common Stock accurately. Notwithstanding, the Committee may determine another appropriate means to determine the Fair Market Value of the initial Stock Option and Restricted Stock Awards on October 2, 2006.

18. **Withholding.** All payments or distributions of Benefits made pursuant to the Plan shall be net of any amounts required to be withheld pursuant to applicable federal, state and local tax withholding requirements. If the Company proposes or is required to distribute Common Stock pursuant to the Plan, it may require the recipient to remit to it or to the corporation that employs such recipient an amount sufficient to satisfy such tax withholding requirements prior to the delivery of any certificates for such Common Stock. In lieu thereof, the Company or the employing corporation shall have the right to withhold the amount of such taxes from any other sums due or to become due from such corporation to the recipient as the Committee shall prescribe. The Committee may, in its discretion and subject to such rules as it may adopt (including any as may be required to satisfy applicable tax and/or non-tax regulatory requirements), permit an optionee or award or right holder to pay all or a portion of the federal, state and local withholding taxes arising in connection with any Benefit consisting of shares of Common Stock by electing to have the Company withhold shares of Common Stock having a Fair Market Value equal to the amount of tax to be withheld, such tax calculated at minimum statutory withholding rates.

19. **Employment Rights.** Neither the Plan nor any action taken hereunder shall be construed as giving any participant the right to be retained in the employ or service of the company or any of its subsidiaries or affiliates.

20. **Unfunded Plan.** Participants shall have no right, title, or interest whatsoever in or to any investments which the Company may make to aid it in meeting its obligations under the Plan. Nothing contained in the Plan, and no action taken pursuant to its provisions, shall create or be construed to create a trust of any kind, or a fiduciary relationship between the Company and any participant, beneficiary, legal representative or any other person. To the extent that any person acquires a right to receive payments from the Company under the Plan, such right shall be no greater than the right of an unsecured general creditor of the Company. All payments to be made hereunder shall be paid from the general funds of the Company and no special or separate fund shall be established and no segregation of assets shall be made to assure payment of such amounts except as expressly set forth in the Plan. The Plan is not intended to be subject to the Employee Retirement Income Security Act of 1974, as amended.

21. **No Fractional Shares.** No fractional shares of Common Stock shall be issued or delivered pursuant to the Plan or any Benefit. The Committee shall determine whether cash, or Benefits, or other property shall be issued or paid in lieu of fractional shares or whether such fractional shares or any rights thereto shall be forfeited or otherwise eliminated.

22. **Duration, Amendment and Termination.** No Benefit shall be granted more than ten (10) years after the Effective Date. The Company may amend the Plan from time to time or suspend or terminate the Plan at any time. No amendment of the Plan may be made without approval of the majority of the shareholders of the Company if the amendment will: (i) increase the aggregate number of shares of Common Stock that may be delivered through Stock Options under the Plan; (ii) increase the maximum number of shares that may be awarded to any participant under Section 5 hereof or the maximum Cash Award that can be paid to any individual under Section 10 hereof; (iii) change the types of business criteria on which Performance-Based Awards are to be based under the Plan; or (iv) modify the requirements as to eligibility for participation in the Plan.

23. **Governing Law.** This Plan, Benefits granted hereunder and actions taken in connection herewith shall be governed and construed in accordance with the laws of the Commonwealth of Pennsylvania (regardless of the law that might otherwise govern under applicable Pennsylvania principles of conflict of laws).

24. **Effective Date.** This Plan is adopted by the Company in anticipation of its emergence from chapter 11 of title 11 of the United States Bankruptcy Code, as a publicly-owned SEC reporting issuer. Stock Options and Restricted Stock Awards provided for in the Company's plan of reorganization will be provided under this Plan. The Plan shall be effective as of the date on which all the conditions to the effectiveness of the Company's plan of reorganization (the "Effective Date", namely October 2, 2006), provided that the Plan is approved by the sole shareholder of the Company on the Effective Date. Such shareholder approval shall be a condition to the right of each participant to receive any Benefits hereunder. Any Benefits granted under the Plan prior to such shareholder approval shall be effective as of the date of grant (unless, with respect to any Benefit, the Committee specifies otherwise at the time of grant), but no such Benefit may be exercised or settled and no restrictions relating to any Benefit may lapse prior to such shareholder approval, and if such shareholder approval is not obtained as provided hereunder, any such Benefit shall be cancelled.

**Armstrong World Industries Inc.**

**2006 Phantom Stock Unit Plan**

*I. Purpose*

The purposes of this 2006 Phantom Stock Unit Plan (the "Plan") are to promote the growth and profitability of Armstrong World Industries, Inc. (the "Corporation") by increasing the mutuality of interests between directors and the shareholders of the Corporation.

*II. Definitions*

The following terms shall have the meanings shown:

1. "Beneficial Owner" shall have the meaning set forth in Rule 13d-3 under the Securities Exchange Act of 1934, as amended (the "Exchange Act").
  2. "Board" shall mean the Board of Directors of the Corporation.
  3. "Change in Control Event" shall mean the occurrence of the event set forth in any one of the following paragraphs with respect to the Corporation:
    - a. Any Person is or becomes the Beneficial Owner, directly or indirectly, of securities of the Corporation (not including in the securities beneficially owned by such Person any securities acquired directly from the Corporation or its affiliates) representing 20% or more of either the then outstanding shares of common stock of the Corporation or the combined voting power of the Corporation's then outstanding securities, excluding any Person who becomes such a Beneficial Owner in connection with a transaction described in clause (i) of paragraph (c) below; or
    - b. The following individuals cease for any reason to constitute a majority of the number of directors then serving: individuals who, on the date hereof, constitute the Board and any new director (other than a director whose initial assumption of office is in connection with an actual or threatened election contest, including but not limited to a consent solicitation, relating to the election of directors of the Corporation) whose appointment or election by the Board or nomination for election by the Corporation's shareholders was approved by a vote of at least two-thirds (2/3) of the directors then still in office who either were directors on the date hereof or whose appointment, election or nomination for election was previously so approved; or
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- c. There is consummated a merger or consolidation of the Corporation (including a triangular merger to which the Corporation is a party) with any other corporation other than (i) a merger or consolidation which would result in the voting securities of the Corporation outstanding immediately prior to such merger or consolidation continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity or any parent thereof) at least 66 2/3% of the combined voting power of the voting securities of the Corporation or such surviving entity or any parent thereof outstanding immediately after such merger or consolidation, or (ii) a merger or consolidation effected to implement a recapitalization of the Corporation (or similar transaction) in which no Person is or becomes the Beneficial Owner, directly or indirectly, of securities of the Corporation (not including in the securities Beneficially Owned by such Person any securities acquired directly from the Corporation or its subsidiaries) representing 20% or more of either the then outstanding shares of common stock of the Corporation or the combined voting power of the Corporation's then outstanding securities; or
  - d. The shareholders of the Corporation approve a plan of complete liquidation or dissolution of the Corporation or there is consummated an agreement for the sale or disposition by the Corporation of all or substantially all of the Corporation's assets, other than a sale or disposition by the Corporation of all or substantially all of the Corporation's assets to an entity, at least 75% of the combined voting power of the voting securities of which are owned by shareholders of the Corporation in substantially the same proportions as their ownership of the Corporation immediately prior to such sale. Notwithstanding the foregoing, no "Change in Control" shall be deemed to have occurred if there is consummated any transaction or series of integrated transactions immediately following which the record holders of the common stock of the Corporation immediately prior to such transaction or series of transactions continue to have substantially the same proportionate ownership in an entity which owns all or substantially all of the assets of the Corporation immediately following such transaction or series of transactions.
- 4. "Committee" shall mean the Nominating and Governance Committee of the Board, or any successor committee.
  - 5. "Common Stock" shall mean Common Stock of the Corporation.
  - 6. "Fair Market Value" shall mean the closing price of the Common Stock on the stock exchange on which the Common Stock is listed on the relevant date, or, if no sale shall have been made on such exchange on that date, the closing price on the following day on which there was a sale.
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7. "Person" shall have the meaning given in Section 3(a)(9) of the Exchange Act, as modified and used in Sections 13(d) and 14(d) thereof, except that such term shall not include (i) the Corporation or any of its subsidiaries, (ii) a trustee or other fiduciary holding securities under an employee benefit plan of the Corporation or any of its subsidiaries, (iii) an underwriter temporarily holding securities pursuant to an offering of such securities, (iv) a corporation owned, directly or indirectly, by the shareholders of the Corporation in substantially the same proportions as their ownership of stock of the Corporation, or (v) an entity or entities which are eligible to file and have filed a Schedule 13G under Rule 13d-1(b) of the Exchange Act, which Schedule indicates beneficial ownership of 15% or more of the outstanding shares of common stock of the Corporation or the combined voting power of the Corporation's then outstanding securities.
  8. "Unit" shall mean a right granted by the Committee pursuant to Section 4.1 to receive the Fair Market Value of a share of Common Stock as of a specified date, which right may be made conditional upon the occurrence or nonoccurrence of other specified events as herein provided.
  9. "Section 409A Change in Control Event" shall mean the first to occur of any of the following events with respect to the Corporation:
    - a. Any one person, or more than one person acting as a group (as determined for purposes of Rule 13d-3 of the Securities Exchange Act of 1934, as amended), acquires ownership of stock of the Corporation that, together with stock held by such person or group, constitutes more than 50% of the total fair market value or total voting power of the stock of the Corporation. However, if any one person, or more than one person acting as a group, is considered to own more than 50% of the total fair market value or total voting power of the stock of the Corporation, the acquisition of additional stock by the same person or persons is not considered to cause a change in the ownership of the Corporation (or to cause a change in the effective control of the corporation (as determined for purposes of Rule 13d-3 of the Securities Exchange Act of 1934, as amended)). An increase in the percentage of stock owned by any one person, or persons acting as a group, as a result of a transaction in which the Corporation acquires its stock in exchange for property will be treated as an acquisition of stock for purposes of this paragraph. This paragraph applies only when there is a transfer of stock of the Corporation (or issuance of stock of the Corporation) and stock in the Corporation remains outstanding after the transaction.
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- b. (i) Any one person, or more than one person acting as a group (as determined for purposes of Rule 13d-3 of the Securities Exchange Act of 1934, as amended), acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) ownership of stock of the Corporation possessing 30% or more of the total voting power of the stock of the Corporation; or (ii) A majority of members of the Corporation's Board of Directors is replaced during any 12-month period by directors whose appointment or election is not endorsed by a majority of the members of the Corporation's Board of Directors before the date of the appointment or election.

Notwithstanding the foregoing, if any one person, or more than one person acting as a group, is considered to effectively control the Corporation (as determined for purposes of Rule 13d-3 of the Securities Exchange Act of 1934, as amended), the acquisition of additional control of the Corporation by the same person or persons is not considered to cause a change in the effective control of the Corporation (or to cause a change in the ownership of the Corporation within the meaning of Treas. Reg. §1.409A-3(i)(5)(v)).

- c. Any one person, or more than one person acting as a group (as determined for purposes of Rule 13d-3 of the Securities Exchange Act of 1934, as amended), acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) assets from the Corporation that have a total gross fair market value equal to or more than 40% of the total gross fair market value of all of the assets of the Corporation immediately before such acquisition or acquisitions. For this purpose, gross fair market value means the value of the assets of the Corporation, or the value of the assets being disposed of, determined without regard to any liabilities associated with such assets. Notwithstanding the foregoing, there is no change in control event when there is a transfer to an entity that is controlled by the shareholders of the Corporation immediately after the transfer. A transfer of assets by the Corporation is not treated as a change in the ownership of such assets if the assets are transferred to: (i) a shareholder of the Corporation (immediately before the asset transfer) in exchange for or with respect to its stock; (ii) an entity, 50% or more of the total value or voting power of which is owned, directly or indirectly, by the Corporation; (iii) a person, or more than one person acting as a group, that owns, directly or indirectly, 50% or more of the total value or voting power of all the outstanding stock of the Corporation; or (iv) an entity, at least 50% of the total value or voting power of which is owned, directly or indirectly, by a person described in (iii) of this paragraph.
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### III. General

1. Administration. The Plan may be administered by the Board or, if delegated, to the Committee, in which case the following provisions would apply:
  - a. Each member of the Committee shall at the time of any action under the Plan be a “disinterested person” as then defined under Rule 16b-3 under the Exchange Act or any successor rule.
  - b. The Committee shall have the authority in its sole discretion from time to time: (i) to award Units to eligible directors as provided herein; (ii) to prescribe such terms, conditions, limitations and restrictions, not inconsistent with the Plan, applicable to any such award as deemed appropriate; and (iii) to interpret the Plan, to adopt, amend and rescind rules and regulations relating to the Plan, and to make all other determinations and take all other action necessary or advisable for the implementation and administration of the Plan. A majority of the Committee shall constitute a quorum, and the action of a majority of the members of the Committee present at any meeting at which a quorum is present, or acts unanimously adopted in writing without the holding of a meeting, shall be the acts of the Committee.
  - c. All such actions shall be final, conclusive and binding upon the participating director. No member of the Committee shall be liable for any action taken or decision made in good faith relating to the Plan or any award thereunder.
2. Eligibility. The Board or the Committee may award Units under the Plan to any outside director of the Corporation.
3. Aggregate Limitation on Awards. The aggregate number of Units which may be awarded under the Plan shall not exceed 150,000 Units, subject to adjustments pursuant to Sections 5.4 and 5.5. If any Unit is surrendered or forfeited to the Corporation for any reason prior to payment thereof, such Unit shall again be available for award under the Plan.

### IV. Units

1. Award of Units. Each outside director of the Corporation shall be awarded the number of Units set forth below, contingent upon their service on the Board in such capacity on the date of award:
    - (a) On October 23, 2006, the number of units equal to (i) \$85,000, divided by (ii) the Fair Market Value of a share of Common Stock on the date of award, rounded to the next highest whole number; and
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- (b) On October 22, 2007, the number of units equal to (i) \$85,000, divided by (ii) the Fair Market Value of a share of Common Stock on the date of award, rounded to the next highest whole number.

In addition, discretionary awards of Units may be made under the Plan.

2. Award Agreements . The award of any Units shall be evidenced by a written agreement executed by the Corporation and the awardee, stating the number of Units awarded and such other terms and conditions of the award as the Board or the Committee may from time to time determine.
3. Optional Terms and Conditions of Units . To the extent not inconsistent with the Plan, the Board or the Committee may prescribe such terms and conditions applicable to any award of Units as it may in its discretion determine; provided, however that the terms and conditions of any award of Units shall be such that the Units shall not constitute “equity securities” of the Corporation for purposes of Section 16 of the Exchange Act.
4. Standard Terms and Conditions of Units . Unless otherwise determined by the Board or the Committee pursuant to Section 4.3, each award of Units shall be made on the following terms and conditions, in addition to such other terms, conditions, limitations and restrictions as the Committee, in its discretion, may determine to prescribe:
  - a. Vesting . The date on which each Unit shall vest, contingent upon the awardee’s continued service as a director of the Corporation on such date, shall be the earlier of:
    - (i) the one-year anniversary of the award of the Units; or
    - (ii) the date of any Change in Control Event.
  - b. Payment Date . The date on which each vested Unit shall become payable (“Payment Date”) shall be the earlier of:
    - (i) the six-month anniversary of the director’s separation from service from the Corporation for any reason other than a removal for cause; or
    - (ii) the date of any Change in Control Event, provided that awardee is a director of the Corporation on such date and that such Change in Control Event also qualifies as a Section 409A Change in Control Event.

Upon the Payment Date, the Corporation shall pay to the awardee in cash an amount equal to the number of vested Units on that date multiplied by the Fair Market Value on the Payment Date of a share of Common Stock.

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- c. Forfeiture of Units . Upon the effective date of a separation of the awardee's service as a director with the Corporation for cause, as determined by the Board or the Committee, all Units for which the Payment Date has not occurred, whether or not vested, shall immediately be forfeited to the Corporation without consideration or further action being required of the Corporation. Upon the effective date of a separation of the awardee's service as a director with the Corporation for any reason other than cause, as determined by the Board or the Committee, all unvested Units shall immediately be forfeited to the Corporation without consideration or further action being required of the Corporation. For purposes of the two immediately preceding sentences, the effective date of the awardee's separation shall be the date on which the awardee ceases to perform services as a director of the Corporation as determined under Section 409A of the Code.
  - d. Dividend Equivalents . If an award of Units is outstanding as of the record date for determination of the shareholders of the Corporation entitled to receive a cash dividend on its outstanding shares of Common Stock, the awardee shall be entitled to a cash payment in an amount equal to (a) the per share amount of such dividend, multiplied by (b) the number of outstanding Units awarded, which amount shall be payable on the six-month anniversary of the awardee's separation from service from the Corporation, without interest.
5. Transfer Restriction . No Unit shall be assignable or transferable by an awardee other than by will, or if the awardee dies intestate, by the laws of descent and distribution of the state of domicile of the awardee at the time of death. All units shall be payable during the lifetime of the awardee.

V. *Miscellaneous*

1. No Right to Continued Service . Nothing in the Plan or in any agreement entered into pursuant to the Plan shall confer upon any awardee the right to continue in the service as a director of the Corporation or affect any right which the Corporation or its shareholders may have to elect or remove directors.
  2. Non-Uniform Determinations . The Board's or Committee's determinations under the Plan need not be uniform and may be made by it selectively among persons who receive, or are eligible to receive, awards under the Plan, whether or not such persons are similarly situated.
  3. No Rights as Shareholders . Recipients of awards under the Plan shall have no rights as shareholders of the Corporation with respect thereto.
  4. Adjustments of Stock . In the event of any change or changes in the outstanding Common Stock, the Board or the Committee may in its discretion appropriately adjust the number of Units which may be awarded under the Plan, the number of Units subject to awards outstanding under the Plan and any and all other matters deemed appropriate by the Committee.
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5. Reorganization . In the event that the outstanding Common Stock shall be changed in number, class or character by reason of any split-up, change of par value, stock dividend, combination or reclassification of shares, merger, consolidation or other corporate change, or shall be changed in value by reason of any spin-off, dividend in partial liquidation or other special distribution, the Board or the Committee shall make such changes as it may deem equitable in outstanding Units awarded pursuant to the Plan and the number and character of Units available for future awards.
6. Amendment or Termination of the Plan . The Committee or the Board may at any time terminate the Plan and may from time to time amend the Plan as it may deem advisable; provided, however, that without shareholder approval, the Board or the Committee may not amend the Plan in a manner which would cause Units to be treated as “equity securities” of the Corporation for purposes of Section 16 of the Exchange Act. The termination or amendment of the Plan shall not, without the consent of the awardee, affect such awardee’s rights under an award previously granted, but may eliminate or reduce any rights or expectation of future awards.

**Armstrong World Industries Inc.**

**2008 Directors Stock Unit Plan**

Adopted by Armstrong World Industries, Inc. Board of Directors on April 11, 2008

*I. Purpose*

The purposes of this 2008 Directors Stock Unit Plan (the "Plan") are to promote the growth and profitability of Armstrong World Industries, Inc. (the "Corporation") by increasing the mutuality of interests between directors and the shareholders of the Corporation.

*II. Definitions*

The following terms shall have the meanings shown:

- 2.1 "Beneficial Owner" shall have the meaning set forth in Rule 13d-3 under the Securities Exchange Act of 1934, as amended (the "Exchange Act").
  - 2.2 "Board" shall mean the Board of Directors of the Corporation.
  - 2.3 "Change in Control Event" shall mean the occurrence of the event set forth in any one of the following paragraphs with respect to the Corporation:
    - (a) Any Person is or becomes the Beneficial Owner, directly or indirectly, of securities of the Corporation (not including in the securities beneficially owned by such Person any securities acquired directly from the Corporation or its affiliates) representing 20% or more of either the then outstanding shares of common stock of the Corporation or the combined voting power of the Corporation's then outstanding securities, excluding any Person who becomes such a Beneficial Owner in connection with a transaction described in clause (i) of paragraph (c) below; or
    - (b) The following individuals cease for any reason to constitute a majority of the number of directors then serving: individuals who, on the date hereof, constitute the Board and any new director (other than a director whose initial assumption of office is in connection with an actual or threatened election contest, including but not limited to a consent solicitation, relating to the election of directors of the Corporation) whose appointment or election by the Board or nomination for election by the Corporation's shareholders was approved by a vote of at least two-thirds (2/3) of the directors then still in office who either were directors on the date hereof or whose appointment, election or nomination for election was previously so approved; or
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- (c) There is consummated a merger or consolidation of the Corporation (including a triangular merger to which the Corporation is a party) with any other corporation other than (i) a merger or consolidation which would result in the voting securities of the Corporation outstanding immediately prior to such merger or consolidation continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity or any parent thereof) at least 66 2/3% of the combined voting power of the voting securities of the Corporation or such surviving entity or any parent thereof outstanding immediately after such merger or consolidation, or (ii) a merger or consolidation effected to implement a recapitalization of the Corporation (or similar transaction) in which no Person is or becomes the Beneficial Owner, directly or indirectly, of securities of the Corporation (not including in the securities Beneficially Owned by such Person any securities acquired directly from the Corporation or its subsidiaries) representing 20% or more of either the then outstanding shares of common stock of the Corporation or the combined voting power of the Corporation's then outstanding securities; or
- (d) The shareholders of the Corporation approve a plan of complete liquidation or dissolution of the Corporation or there is consummated an agreement for the sale or disposition by the Corporation of all or substantially all of the Corporation's assets, other than a sale or disposition by the Corporation of all or substantially all of the Corporation's assets to an entity, at least 75% of the combined voting power of the voting securities of which are owned by shareholders of the Corporation in substantially the same proportions as their ownership of the Corporation immediately prior to such sale. Notwithstanding the foregoing, no "Change in Control" shall be deemed to have occurred if there is consummated any transaction or series of integrated transactions immediately following which the record holders of the common stock of the Corporation immediately prior to such transaction or series of transactions continue to have substantially the same proportionate ownership in an entity which owns all or substantially all of the assets of the Corporation immediately following such transaction or series of transactions.

2.4 "Committee" shall mean the Nominating and Governance Committee of the Board, or any successor committee.

2.5 "Common Stock" shall mean Common Stock of the Corporation.

2.6 "Delivery Date" shall have the meaning set forth in Section 4.4(b).

2.7 "Fair Market Value" shall mean the closing price of the Common Stock on the stock exchange on which the Common Stock is listed on the relevant date, or, if no sale shall have been made on such exchange on that date, the closing price on the following day on which there was a sale.

2.8 "Participant" shall mean a non-employee director to whom Units are granted under the Plan.

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- 2.9 “Person” shall have the meaning given in Section 3(a)(9) of the Exchange Act, as modified and used in Sections 13(d) and 14(d) thereof, except that such term shall not include (i) the Corporation or any of its subsidiaries, (ii) a trustee or other fiduciary holding securities under an employee benefit plan of the Corporation or any of its subsidiaries, (iii) an underwriter temporarily holding securities pursuant to an offering of such securities, (iv) a corporation owned, directly or indirectly, by the shareholders of the Corporation in substantially the same proportions as their ownership of stock of the Corporation, or (v) an entity or entities which are eligible to file and have filed a Schedule 13G under Rule 13d-1(b) of the Exchange Act, which Schedule indicates beneficial ownership of 15% or more of the outstanding shares of common stock of the Corporation or the combined voting power of the Corporation’s then outstanding securities.
- 2.10 “Unit” shall mean a right granted by the Committee pursuant to Section 4.1 to receive one share of Common Stock as of a specified date, which right may be made conditional upon the occurrence or nonoccurrence of other specified events as herein provided.
- 2.11 “Section 409A Change in Control Event” shall mean the first to occur of any of the following events with respect to the Corporation:
- (a) Any one person, or more than one person acting as a group (as determined for purposes of 13d-3 of the Securities Exchange Act of 1934, as amended), acquires ownership of stock of the Corporation that, together with stock held by such person or group, constitutes more than 50% of the total fair market value or total voting power of the stock of the Corporation. However, if any one person, or more than one person acting as a group, is considered to own more than 50% of the total fair market value or total voting power of the stock of the Corporation, the acquisition of additional stock by the same person or persons is not considered to cause a change in the ownership of the Corporation (or to cause a change in the effective control of the corporation (as determined for purposes of 13d-3 of the Securities Exchange Act of 1934, as amended)). An increase in the percentage of stock owned by any one person, or persons acting as a group, as a result of a transaction in which the Corporation acquires its stock in exchange for property will be treated as an acquisition of stock for purposes of this paragraph. This paragraph applies only when there is a transfer of stock of the Corporation (or issuance of stock of the Corporation) and stock in the Corporation remains outstanding after the transaction.
  - (b) (i) Any one person, or more than one person acting as a group (as determined for purposes of 13d-3 of the Securities Exchange Act of 1934, as amended), acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) ownership of stock of the Corporation possessing 30% or more of the total voting power of the stock of the Corporation; or (ii) A majority of members of the Corporation’s Board of Directors is replaced during any 12-month period by directors whose appointment or election is not endorsed by a majority of the members of the Corporation’s Board of Directors before the date of the appointment or election.
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Notwithstanding the foregoing, if any one person, or more than one person acting as a group, is considered to effectively control the Corporation (as determined for purposes of 13d-3 of the Securities Exchange Act of 1934, as amended), the acquisition of additional control of the Corporation by the same person or persons is not considered to cause a change in the effective control of the Corporation (or to cause a change in the ownership of the Corporation within the meaning of Treas. Reg. §1.409A-3(i)(5)(v)).

- (c) Any one person, or more than one person acting as a group (as determined for purposes of 13d-3 of the Securities Exchange Act of 1934, as amended), acquires (or has acquired during the 12-month period ending on the date of the most recent acquisition by such person or persons) assets from the Corporation that have a total gross fair market value equal to or more than 40% of the total gross fair market value of all of the assets of the Corporation immediately before such acquisition or acquisitions. For this purpose, gross fair market value means the value of the assets of the Corporation, or the value of the assets being disposed of, determined without regard to any liabilities associated with such assets. Notwithstanding the foregoing, there is no change in control event when there is a transfer to an entity that is controlled by the shareholders of the Corporation immediately after the transfer. A transfer of assets by the Corporation is not treated as a change in the ownership of such assets if the assets are transferred to: (i) a shareholder of the Corporation (immediately before the asset transfer) in exchange for or with respect to its stock; (ii) an entity, 50% or more of the total value or voting power of which is owned, directly or indirectly, by the Corporation; (iii) a person, or more than one person acting as a group, that owns, directly or indirectly, 50% or more of the total value or voting power of all the outstanding stock of the Corporation; or (iv) an entity, at least 50% of the total value or voting power of which is owned, directly or indirectly, by a person described in (iii) of this paragraph.

### *III. General*

- 3.1 Administration . The Plan may be administered by the Board or, if delegated, to the Committee. Administration shall be delegable to the extent provided by law. If authority is delegated to the Committee, the following provisions would apply:
    - (a) Each member of the Committee shall at the time of any action under the Plan be a “disinterested person” as then defined under Rule 16b-3 under the Exchange Act or any successor rule.
    - (b) The Committee shall have the authority in its sole discretion from time to time: (i) to make discretionary grants of Units to eligible directors as provided herein; (ii) to prescribe such terms, conditions, limitations and restrictions, not inconsistent with the Plan, applicable to any grant as deemed appropriate; and (iii) to interpret the Plan, to adopt, amend and rescind rules and regulations relating to the Plan, and to make all other determinations and take all other action necessary or advisable for the implementation and administration of the Plan. A majority of the Committee shall constitute a quorum, and the action of a majority of the members of the Committee present at any meeting at which a quorum is present, or acts unanimously adopted in writing without the holding of a meeting, shall be the acts of the Committee.
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(c) All such actions shall be final, conclusive and binding upon the Participant. No member of the Committee shall be liable for any action taken or decision made in good faith relating to the Plan or any grant thereunder.

- 3.2 Eligibility. A grant of Units under the Plan may be made to any non-employee director of the Corporation.
- 3.3 Aggregate Limit on Grants. The aggregate number of shares of Common Stock which may be issued in connection with Units granted under the Plan shall not exceed 300,000 shares, subject to adjustments pursuant to Sections 5.4 and 5.5. Shares subject to grants under this Plan may either be authorized but unissued shares or previously issued shares that have been reacquired by the Corporation. Shares authorized under the Plan may be used to satisfy obligations of the Corporation for units granted under the 2006 Phantom Stock Unit Plan based upon election by Participants holding such units.
- 3.4 Election to Satisfy Units under the 2006 Plan. Participants who hold units granted under the 2006 Phantom Stock Unit Plan may elect to have the Corporation satisfy its payment obligations in respect of such units in the same manner in which the Corporation satisfies its payment obligations for units granted under this Plan, e.g., by delivering one share of common stock for each unit granted under that plan out of the reserve for shares authorized for issuance under this Plan. Payments to Participants who have made such election in respect of units under that 2006 Plan will be made according to the terms of this Plan.
- 3.5 Term. Grants under this Plan may be made through October 2017. No further grants may be made after that date unless shareholders have approved an extension of the Plan.

#### *IV. Units*

- 4.1 Grant of Units. Each non-employee director of the Corporation shall be granted the number of Units set forth below, contingent upon their service on the Board in such capacity on the date of grant:
- (a) Annual Grants. On the first business day following the regular meeting of the Board each October (or if there is no regular meeting scheduled in that month, then the last business day of that month), each non-employee director shall be granted a number of Units equal to (i) 55% of the total compensation payable to the non-employee director as an annual retainer divided by (ii) the Fair Market Value of a share of Common Stock on that date, rounded to the next highest whole number.
- (b) Discretionary Grants. Units may also be granted at such times, and in amounts to such eligible non-employee directors, upon such terms and conditions as are deemed appropriate.
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- 4.2 Grant Agreements . The grant of any Units shall be evidenced by a written agreement executed by the Corporation and the Participant, stating the number of Units granted and such other terms and conditions of the grant as the Board or the Committee may from time to time determine. The Plan has been written with the intent of complying with Section 409A of the U.S. Internal Revenue Code. However, if any grant shall be deemed to constitute a deferral of compensation subject to said section, in the discretion of the Committee, the grant may be unilaterally modified to comply with the requirements of said section or cancelled.
- 4.3 Optional Terms and Conditions of Units . To the extent not inconsistent with the Plan, the Board or the Committee may prescribe such terms and conditions applicable to any grant of Units as it may in its discretion determine.
- 4.4 Standard Terms and Conditions of Units . Unless otherwise determined by the Board or the Committee pursuant to Section 4.3, each grant of Units shall be made on the following terms and conditions, in addition to such other terms, conditions, limitations and restrictions as the Board or Committee, in its discretion, may determine to prescribe:
- (a) Vesting . The date on which each Unit shall vest, contingent upon the Participant's continued service as a director of the Corporation on such date, shall be the earlier of:
- (i) the one-year anniversary of the grant;
  - (ii) the death or total and permanent disability of the Participant; or
  - (iii) the date of any Change in Control Event.
- (b) Delivery Date . The date on which each vested Unit shall be paid ("Delivery Date") shall be the earlier of:
- (i) the six-month anniversary of the director's separation from service from the Corporation for any reason other than a removal for cause; or
  - (ii) the date of any Change in Control Event, provided that Participant is a director of the Corporation on such date and that such Change in Control Event also qualifies as a Section 409A Change in Control Event.

Upon the Delivery Date, the Corporation shall deliver to the Participant shares of Common Stock in payment for the vested Units, with one share of Common Stock delivered for each vested Unit.

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- (c) Forfeiture of Units . Upon the effective date of a separation of the Participant's service as a director with the Corporation for cause, as determined by the Board or the Committee, all Units for which the Delivery Date has not occurred, whether or not vested, shall immediately be forfeited to the Corporation without consideration or further action being required of the Corporation. Upon the effective date of a separation of the Participant's service as a director with the Corporation for any reason other than cause, as determined by the Board or the Committee, all unvested Units shall immediately be forfeited to the Corporation without consideration or further action being required of the Corporation. For purposes of the two immediately preceding sentences, the effective date of the Participant's separation shall be the date on which the Participant ceases to perform services as a director of the Corporation as determined under Section 409A of the Code.
- (d) Dividend Equivalents . If an award of Units is outstanding as of the record date for determination of the shareholders of the Corporation entitled to receive a cash dividend on its outstanding shares of Common Stock, the awardee shall be entitled to a cash payment in an amount equal to (a) the per share amount of such dividend, multiplied by (b) the number of outstanding Units awarded to be paid on the payment date for such dividend, provided the Participant is serving as a director of the Corporation on such date.

4.5 Transfer Restriction . No Unit shall be assignable or transferable by another than by will, or if the Participant dies intestate, by the laws of descent and distribution of the state of domicile at the time of death.

#### *V. Miscellaneous*

- 5.1 No Right to Continued Service . Nothing in the Plan or in any agreement entered into pursuant to the Plan shall confer upon any Participant the right to continue in the service as a director of the Corporation or affect any right which the Corporation or its shareholders may have to elect or remove directors.
  - 5.2 Non-Uniform Determinations . The Board's or Committee's determinations under the Plan need not be uniform and may be made by it selectively among persons who receive, or are eligible to receive, grants under the Plan, whether or not such persons are similarly situated.
  - 5.3 No Rights as Shareholders . Recipients of grants under the Plan shall have no rights as shareholders of the Corporation with respect thereto until shares of Common Stock are delivered in payment therefor.
  - 5.4 Adjustments of Stock . In the event of any change or changes in the outstanding Common Stock, the Committee shall in its discretion appropriately adjust the number of Units which may be granted under the Plan, the number of Units subject to grants made under the Plan and any and all other matters deemed appropriate by the Committee.
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- 5.5 Reorganization . In the event that the outstanding Common Stock shall be changed in number, class or character by reason of any split-up, change of par value, stock dividend, combination or reclassification of shares, merger, consolidation or other corporate change, or shall be changed in value by reason of any spin-off, dividend in partial liquidation or other special distribution, the Board or the Committee shall make such changes as it may deem equitable in outstanding Units granted pursuant to the Plan and the number and character of Units available for future grants.
- 5.6 Amendment or Termination of the Plan . The Board may at any time terminate the Plan and may from time to time amend the Plan as it may deem advisable; provided, however, that approval of the shareholders of the Corporation will be required for any amendment:
- (a) To increase the total number of shares issuable under the Plan under Section 3.3 (except for adjustments under Section 5.4 or 5.5); or
  - (b) That would otherwise constitute a “material revision” within the meaning of applicable rules of the New York Stock Exchange in effect at that time.

An amendment of this Plan will, unless the amendment provides otherwise, be immediately and automatically effective for all outstanding grants. The Board may also amend any outstanding grants under this Plan, provided the grants, as amended, contain only such terms and conditions as would be permitted or required for a new grant under this Plan.

- 5.7 Governing Law . This Plan will be governed by the laws of the Commonwealth of Pennsylvania, without regard to any conflict of law rules.

## ARMSTRONG WORLD INDUSTRIES, INC. AND SUBSIDIARIES

COMPUTATION OF EARNINGS PER SHARE  
(AMOUNTS IN MILLIONS EXCEPT FOR PER-SHARE DATA)

	Year Ended December 31, 2008	Year Ended December 31, 2007	Three Months Ended December 31, 2006	Nine Months Ended September 30, 2006
<b>Basic earnings per share</b>				
Net earnings	\$ 81.0	\$ 145.3	\$ 2.2	n/a
Basic weighted average number of common shares outstanding	56.4	56.0	55.0	n/a
Basic earnings per share	\$ 1.44	\$ 2.59	\$ 0.04	n/a
<b>Diluted earnings per share</b>				
Net earnings	\$ 81.0	\$ 145.3	\$ 2.2	n/a
Basic weighted average number of common shares outstanding	56.4	56.0	55.0	n/a
Weighted average number of common shares issuable under stock option or unvested stock grants	0.2	0.7	0.3	n/a
Diluted weighted average number of common shares outstanding	56.6	56.7	55.3	n/a
Diluted earnings per share	\$ 1.43	\$ 2.56	\$ 0.04	n/a

**Subsidiaries of Armstrong World Industries, Inc.  
As of February 26, 2009**

The following is a list of subsidiaries of Armstrong World Industries, Inc., omitting certain subsidiaries, which, considered in the aggregate as a single subsidiary, would not constitute a significant subsidiary.

U.S. Subsidiaries	Jurisdiction of Incorporation
Armstrong Cork Finance LLC	Delaware
Armstrong NW LLC	Delaware
Armstrong Hardwood Flooring Company	Tennessee
Armstrong Realty Group, Inc.	Pennsylvania
Armstrong Ventures, Inc.	Delaware
Armstrong Wood Products, Inc.	Delaware
Armstrong World Industries (Delaware) LLC	Delaware
AWI Licensing Company	Delaware
HomerWood Hardwood Flooring Company	Delaware
Patriot Flooring Supply, Inc.	Delaware
Worthington Armstrong Venture (50% owned Delaware General Partnership)	
Non-U.S. Subsidiaries	Jurisdiction of Incorporation
Armstrong (U.K.) Investments	United Kingdom
Armstrong Architectural Products S.L.	Spain
Armstrong Building Products B.V.	Netherlands
Armstrong Building Products Company (Shanghai) Ltd. (80% owned affiliate)	PRC
Armstrong Building Products GmbH	Germany
Armstrong DLW AG	Germany
Armstrong DLW Licensing GmbH	Germany
Armstrong Metal Ceilings Limited	United Kingdom
Armstrong Metalldecken AG	Switzerland
Armstrong Metalldecken GmbH	Austria
Armstrong Metalldecken Holdings AG	Switzerland
Armstrong World Industries (Australia) Pty. Ltd.	Australia
Armstrong World Industries AB	Sweden
Armstrong World Industries Canada Ltd.	Canada
Armstrong World Industries Holding GmbH	Germany
Armstrong World Industries Ltd.	United Kingdom

Consent of Independent Registered Public Accounting Firm

The Board of Directors  
Armstrong World Industries, Inc.:

We consent to the incorporation by reference in Registration Statement No. 333-138034 on Form S-8 of Armstrong World Industries, Inc. of our reports dated February 25, 2009, with respect to the consolidated balance sheets of Armstrong World Industries, Inc. and subsidiaries as of December 31, 2008 and 2007 for the Successor Company, and the related consolidated statements of earnings, cash flows and shareholders' equity and the related financial statement schedule for the years ended December 31, 2008 and 2007 and three months ended December 31, 2006 for the Successor Company and the nine months ended September 30, 2006 for the Predecessor Company, and the effectiveness of internal control over financial reporting as of December 31, 2008, which reports appear in the December 31, 2008 annual report on Form 10-K of Armstrong World Industries, Inc.

Our report on the consolidated financial statements and financial statement schedule dated February 25, 2009, contains a paragraph that states Armstrong World Industries, Inc. emerged from the Chapter 11 bankruptcy proceeding. In connection with its emergence from the Chapter 11 bankruptcy proceeding, the Company adopted fresh-start reporting pursuant to Statement of Position 90-7, "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code" as of October 2, 2006. As a result, the financial statements of the Successor Company are presented on a different basis than those of the Predecessor Company and, therefore, are not comparable in all respects. The Company has reflected the effects of the Plan and fresh-start reporting in the Predecessor Company for the nine month period ended September 30, 2006. Our report dated February 25, 2009 also states that, upon adoption of fresh-start reporting, the Company adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109" and Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106, and 132(R)."

/s/ KPMG LLP

Philadelphia, Pennsylvania  
February 25, 2009

Consent of Independent Registered Public Accounting Firm

The Board of Directors  
Worthington Armstrong Venture:

We consent to the incorporation by reference in Registration Statement No. 333-138034 on Form S-8 of Armstrong World Industries, Inc. of our report dated February 20, 2009, with respect to the consolidated balance sheets of Worthington Armstrong Venture and subsidiaries as of December 31, 2008 and 2007 and the related consolidated statements of income, partners' equity (deficit) and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2008, which report is included in the December 31, 2008 annual report on Form 10-K of Armstrong World Industries, Inc.

/s/ KPMG LLP

Harrisburg, Pennsylvania  
February 20, 2009



ARMSTRONG WORLD INDUSTRIES, INC.  
CERTIFICATION REGARDING  
POWER OF ATTORNEY

I, Jeffrey D. Nickel, Senior Vice President, Secretary and General Counsel of Armstrong World Industries, Inc., a corporation organized and existing under the laws of the Commonwealth of Pennsylvania, do hereby certify that at a meeting of the Board of Directors of said corporation duly held on the 23rd day of February, 2009, at which a quorum was present and acting throughout, the following resolution was adopted and is now in full force and effect.

RESOLVED that the execution of the Company's 2008 Annual Report on Form 10-K on behalf of the Company and by members of the Board of Directors through respective powers of attorney granting Michael D. Lockhart, Jeffrey D. Nickel and Michele M. Nicholas the power to sign on their behalf is authorized.

IN WITNESS WHEREOF, I have hereunto set my hand and the seal of said corporation this 23rd day of February, 2009.

/s/ Jeffrey D. Nickel  
Jeffrey D. Nickel  
Senior Vice President, Secretary and  
General Counsel

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**ARMSTRONG WORLD INDUSTRIES, INC.****POWER OF ATTORNEY**

RE: 2008 ANNUAL REPORT ON FORM 10-K

I, Michael D. Lockhart, as a Director of Armstrong World Industries, Inc., do hereby constitute and appoint, JEFFREY D. NICKEL or, in the case of his absence or inability to act as such, MICHELE M. NICHOLAS, my agent, to sign in my name and on my behalf the Company's Annual Report on Form 10-K for the year ended December 31, 2008, and any amendments thereto, to be filed by the Company with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended, with the same effect as if such signature were made by me personally.

/s/ Michael D. Lockhart

Michael D. Lockhart

Dated: February 23, 2009

Each of the undersigned hereby constitutes and appoints, MICHAEL D. LOCKHART or, in the case of his absence or inability to act as such, JEFFREY D. NICKEL or, in the case of his absence or inability to act as such, MICHELE M. NICHOLAS, as attorney-in-fact, for her or for him, to sign the Company's Annual Report on Form 10-K for the year ended December 31, 2008, and any amendments thereto, to be filed by the Company with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended, with the same effect as if each signed personally.

Pursuant to the Securities and Exchange Act of 1934, as amended, this Report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Stanley A. Askren	Director	February 23, 2009
Jon A. Boscia	Director	February 23, 2009
James J. Gaffney	Director	February 23, 2009
Robert C. Garland	Director	February 23, 2009
Judith R. Haberkorn	Director	February 23, 2009
James J. O'Connor	Director	February 23, 2009
Russell F. Peppet	Director	February 23, 2009
Arthur J. Pergament	Director	February 23, 2009
John J. Roberts	Director	February 23, 2009
Alexander M. Sanders, Jr.	Director	February 23, 2009

I, Michael D. Lockhart, certify that:

- 1) I have reviewed this report on Form 10-K of Armstrong World Industries, 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 and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) or 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 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 function):
  - 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 controls over financial reporting.

Date: February 26, 2009

/s/ Michael D. Lockhart  
\_\_\_\_\_  
Michael D. Lockhart  
Chairman and Chief Executive Officer

I, F. Nicholas Grasberger III, certify that:

- 1) I have reviewed this report on Form 10-K of Armstrong World Industries, 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 and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) or 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 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 function):
  - 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 controls over financial reporting.

Date: February 26, 2009

/s/ F. Nicholas Grasberger III  
F. Nicholas Grasberger III  
Senior Vice President and Chief Financial Officer

Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, filed herewith.

Armstrong World Industries, Inc.  
(the "Company")

*Written Statement by Chief Executive Officer*  
Pursuant to Section 906 of Sarbanes-Oxley Act of 2002

I certify to the best of my knowledge and belief that the Company's Form 10-K annual report containing its financial statements for the fiscal year ended December 31, 2008 fully complies with the requirements of section 13(a) of the Securities Exchange Act of 1934, and that information contained in that report fairly presents, in all material respects, the financial condition and results of operations of the Company as of that date.

/s/ Michael D. Lockhart

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Michael D. Lockhart  
Chairman and Chief Executive Officer  
Armstrong World Industries, Inc.

Dated: February 26, 2009

Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, filed herewith.

Armstrong World Industries, Inc.  
(the "Company")

*Written Statement by Chief Financial Officer*  
Pursuant to Section 906 of Sarbanes-Oxley Act of 2002

I certify to the best of my knowledge and belief that the Company's Form 10-K annual report containing its financial statements for the fiscal year ended December 31, 2008 fully complies with the requirements of section 13(a) of the Securities Exchange Act of 1934, and that information contained in that report fairly presents, in all material respects, the financial condition and results of operations of the Company as of that date.

/s/ F. Nicholas Grasberger III

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F. Nicholas Grasberger III  
Senior Vice President and Chief Financial Officer  
Armstrong World Industries, Inc.

Dated: February 26, 2009

**WORTHINGTON ARMSTRONG VENTURE**

Consolidated Financial Statements

December 31, 2008 and 2007

(With Independent Auditors' Report Thereon)

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# WORTHINGTON ARMSTRONG VENTURE

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## Independent Auditors' Report

The Board of Directors  
Worthington Armstrong Venture:

We have audited the accompanying consolidated balance sheets of Worthington Armstrong Venture and subsidiaries (a general partnership) (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of income, partners' equity (deficit) and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Worthington Armstrong Venture and subsidiaries as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

Harrisburg, Pennsylvania  
February 20, 2009

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**WORTHINGTON ARMSTRONG VENTURE**

## Consolidated Balance Sheets

December 31, 2008 and 2007

(In thousands)

	<u>2008</u>	<u>2007</u>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 50,284	47,304
Accounts receivable, net	33,946	45,876
Inventory, net	46,636	36,283
Other current assets	<u>1,595</u>	<u>1,511</u>
Total current assets	132,461	130,974
Property, plant, and equipment, net	30,081	28,192
Goodwill	2,230	2,278
Other assets	<u>461</u>	<u>500</u>
Total assets	<u>\$ 165,233</u>	<u>161,944</u>
<b>Liabilities and Partners' Equity (Deficit)</b>		
Current liabilities:		
Accounts payable	\$ 12,745	17,774
Accrued expenses	6,837	10,419
Taxes payable	<u>2,024</u>	<u>741</u>
Total current liabilities	<u>21,606</u>	<u>28,934</u>
Long-term liabilities:		
Deferred income taxes	583	673
Long-term debt	150,000	100,000
Other long-term liabilities	<u>6,204</u>	<u>3,467</u>
Total long-term liabilities	<u>156,787</u>	<u>104,140</u>
Total liabilities	<u>178,393</u>	<u>133,074</u>
Partners' equity (deficit):		
Contributed capital	—	22,438
Retained earnings	—	—
Distributions in excess of earnings and contributions	(13,117)	—
Accumulated other comprehensive income (loss)	<u>(43)</u>	<u>6,432</u>
Total partners' equity (deficit)	<u>(13,160)</u>	<u>28,870</u>
Total liabilities and partners' equity (deficit)	<u>\$ 165,233</u>	<u>161,944</u>

See accompanying notes to consolidated financial statements.

## WORTHINGTON ARMSTRONG VENTURE

### Consolidated Statements of Income

Years ended December 31, 2008, 2007, and 2006

(In thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Net sales	\$ 421,836	379,988	348,811
Cost of sales	<u>(261,664)</u>	<u>(245,061)</u>	<u>(224,735)</u>
Gross margin	160,172	134,927	124,076
Selling, general, and administrative expenses	<u>(27,349)</u>	<u>(22,310)</u>	<u>(19,038)</u>
	132,823	112,617	105,038
Other income	108	114	100
Interest income	1,501	2,162	3,679
Interest expense	<u>(3,965)</u>	<u>(4,400)</u>	<u>(177)</u>
Income before income tax expense	130,467	110,493	108,640
Income tax expense	<u>(5,022)</u>	<u>(3,450)</u>	<u>(3,754)</u>
Net income	<u>\$ 125,445</u>	<u>107,043</u>	<u>104,886</u>

See accompanying notes to consolidated financial statements.

## WORTHINGTON ARMSTRONG VENTURE

### Consolidated Statements of Partners' Equity (Deficit) and Comprehensive Income

Years ended December 31, 2008, 2007, and 2006

(In thousands)

	<u>Contributed capital</u>		<u>Retained earnings</u>	<u>Distributions in excess of earnings and contributions</u>	<u>Accumulated other comprehensive income (loss)</u>	<u>Total partners' equity (deficit)</u>	<u>Comprehensive income</u>
	<u>Armstrong Ventures, Inc.</u>	<u>The Worthington Steel Company</u>					
Balance, January 1, 2006	\$ 12,925	9,713	108,871	—	(557)	130,952	<u>\$ 74,510</u>
Net income	—	—	104,886	—	—	104,886	\$ 104,886
Distributions	—	—	(86,000)	—	—	(86,000)	—
Reduction in minimum pension liability	—	—	—	—	40	40	40
Foreign currency translation adjustments	—	—	—	—	3,072	3,072	3,072
Balance, December 31, 2006	12,925	9,713	127,757	—	2,555	152,950	<u>\$ 107,998</u>
Net income	—	—	107,043	—	—	107,043	\$ 107,043
Distributions	(100)	(100)	(234,800)	—	—	(235,000)	—
Change in funded status of pension plan	—	—	—	—	252	252	252
Foreign currency translation adjustments	—	—	—	—	3,625	3,625	3,625
Balance, December 31, 2007	12,825	9,613	—	—	6,432	28,870	<u>\$ 110,920</u>
Net income	—	—	125,445	—	—	125,445	\$ 125,445
Distributions	(12,825)	(9,613)	(125,445)	(13,117)	—	(161,000)	—
Change in funded status of pension plan	—	—	—	—	(2,217)	(2,217)	(2,217)
Foreign currency translation adjustments	—	—	—	—	(4,258)	(4,258)	(4,258)
Balance, December 31, 2008	<u>\$ —</u>	<u>—</u>	<u>—</u>	<u>(13,117)</u>	<u>(43)</u>	<u>(13,160)</u>	<u>\$ 118,970</u>

See accompanying notes to consolidated financial statements.

**WORTHINGTON ARMSTRONG VENTURE**

Consolidated Statements of Cash Flows

Years ended December 31, 2008, 2007, and 2006

(In thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>
<b>Cash flows from operating activities:</b>			
Net income	\$ 125,445	107,043	104,886
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	3,648	3,276	4,367
Deferred income taxes	69	53	11
Change in accounts receivable	11,714	974	(7,768)
Change in inventory	(11,385)	3,632	(8,660)
Change in accounts payable and accrued expenses	(7,491)	(400)	7,258
Other	<u>(1,367)</u>	<u>(547)</u>	<u>803</u>
Net cash provided by operating activities	<u>120,633</u>	<u>114,031</u>	<u>100,897</u>
<b>Cash flows from investing activities:</b>			
Purchases of property, plant, and equipment	(6,272)	(5,051)	(2,556)
Sale of property, plant, and equipment	<u>75</u>	<u>—</u>	<u>13</u>
Net cash used in investing activities	<u>(6,197)</u>	<u>(5,051)</u>	<u>(2,543)</u>
<b>Cash flows from financing activities:</b>			
Issuance of long-term debt	50,000	100,000	—
Distributions paid	(161,000)	(235,000)	(86,000)
Issuance costs related to debt	<u>—</u>	<u>(232)</u>	<u>—</u>
Net cash used in financing activities	<u>(111,000)</u>	<u>(135,232)</u>	<u>(86,000)</u>
Effect of exchange rate changes on cash and cash equivalents	<u>(456)</u>	<u>1,531</u>	<u>981</u>
Net increase (decrease) in cash and cash equivalents	2,980	(24,721)	13,335
Cash and cash equivalents at beginning of year	<u>47,304</u>	<u>72,025</u>	<u>58,690</u>
Cash and cash equivalents at end of year	<u>\$ 50,284</u>	<u>47,304</u>	<u>72,025</u>
<b>Supplemental disclosures:</b>			
Interest paid	\$ 4,530	2,590	102
Income taxes paid	3,423	3,937	2,221

See accompanying notes to consolidated financial statements.

## WORTHINGTON ARMSTRONG VENTURE

### Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

#### (1) Description of Business

Worthington Armstrong Venture (the Company) is a general partnership, formed in June 1992, between Armstrong Ventures, Inc. (Armstrong), a subsidiary of Armstrong World Industries, Inc., and The Worthington Steel Company (Worthington), a Delaware corporation (a subsidiary of Worthington Industries, Inc.). Its business is to manufacture and market suspension systems for commercial and residential ceiling markets throughout the world. The Company has manufacturing plants located in the United States, France, Spain, the United Kingdom, and the Peoples Republic of China.

#### (2) Summary of Significant Accounting Policies

##### (a) Use of Estimates

These consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and include management estimates and judgments, where appropriate. Significant items subject to such estimates and assumptions include the carrying amount of property, plant, and equipment and goodwill; valuation allowances for receivables and inventories; and assets and obligations related to employee benefits. Actual results could differ from those estimates.

##### (b) Consolidation Policy

The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany transactions have been eliminated.

##### (c) Revenue Recognition

The Company recognizes revenue from the sale of products and the related accounts receivable when title transfers, generally on the date of shipment. At the time of shipment, a provision is made for estimated applicable discounts and losses that reduce revenue. Sales with independent U.S. distributors of products to major home center retailers are recorded when the products are shipped from the distributor's locations to these retailers. Sales taxes collected from customers and remitted to governmental authorities are accounted for on a net basis and, therefore, are excluded from revenues in the consolidated statements of income.

##### (d) Advertising Costs

The Company recognizes advertising expense as incurred. Advertising expense was \$1,193, \$970 and \$849 for the years ended December 31, 2008, 2007, and 2006, respectively.

##### (e) Research and Development Expenditures

The Company recognizes research and development expense as expenditures are incurred. Total research and development expense was \$4,762, \$3,734 and \$2,805 for the years ended December 31, 2008, 2007, and 2006, respectively.

(Continued)

## WORTHINGTON ARMSTRONG VENTURE

### Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

**(f) Taxes**

The Company is a general partnership in the United States and, accordingly, generally, U.S. federal and state income taxes are the responsibility of the two general partners. Deferred income tax assets and liabilities are recognized for foreign subsidiaries for taxes estimated to be payable in future years based upon differences between the financial reporting and tax bases of assets and liabilities. Deferred tax assets and liabilities are determined using enacted rates expected to apply to taxable income in the years the temporary differences are expected to be recovered or settled. The Company has deferred the application of Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, in accordance with FASB Staff Position FIN 48-3, *Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises*. The Company's current policy is to recognize the effect of income tax positions only if such positions are probable of being sustained.

**(g) Cash and Cash Equivalents**

Short-term cash investments that have maturities of three months or less when purchased are considered to be cash equivalents.

**(h) Trade Accounts Receivable**

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The Company maintains an allowance for doubtful accounts for estimated losses inherent in its accounts receivable portfolio. In establishing the required allowance, management considers historical losses, current receivables aging, and existing industry and national economic data. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Company does not have any off-balance-sheet credit exposure related to its customers.

**(i) Inventories**

Inventories are valued at the lower of cost or market. Cost is determined on the first-in, first-out method.

**(j) Long-Lived Assets**

Property, plant, and equipment are stated at cost, with accumulated depreciation and amortization deducted to arrive at net book value. Depreciation charges are determined generally on the straight-line basis over the useful lives as follows: buildings, 30 years; machinery and equipment, 5 to 15 years; and leasehold improvements over the shorter of 10 years or the life of the lease. Impairment losses are recorded when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. If an impairment exists, the asset is reduced to fair value.

(Continued)

## WORTHINGTON ARMSTRONG VENTURE

### Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

**(k) Goodwill**

Goodwill is tested for impairment at least annually. The impairment tests performed in 2008, 2007, and 2006 did not result in an impairment of the Company's goodwill.

**(l) Foreign Currency Translation and Transactions**

For subsidiaries with functional currencies other than the U.S. dollar, income statement items are translated into dollars at average exchange rates throughout the year and balance sheet items are translated at year-end exchange rates. Gains or losses on foreign currency transactions are recognized in other income, net in the accompanying consolidated statements of income. Gains and losses on foreign translation are recognized in accumulated other comprehensive income in the accompanying consolidated balance sheets.

**(3) Accounts Receivable**

The Company sells its products to select, preapproved customers whose businesses are directly affected by changes in economic and market conditions. The Company considers these factors and the financial condition of each customer when establishing its allowance for losses from doubtful accounts. The allowance for doubtful accounts was \$223 and \$283 at December 31, 2008 and 2007, respectively.

**(4) Inventory**

	<u>2008</u>	<u>2007</u>
Finished goods	\$ 20,288	15,446
Goods in process	139	120
Raw materials	22,997	17,323
Supplies	<u>3,212</u>	<u>3,394</u>
Total inventories	<u>\$ 46,636</u>	<u>36,283</u>

**(5) Property, Plant, and Equipment**

	<u>2008</u>	<u>2007</u>
Land	\$ 1,911	1,407
Buildings	13,536	13,716
Machinery and equipment	66,714	66,816
Computer software	733	713
Construction in process	<u>5,706</u>	<u>4,167</u>
	88,600	86,819
Accumulated depreciation and amortization	<u>(58,519)</u>	<u>(58,627)</u>
Total property, plant, and equipment, net	<u>\$ 30,081</u>	<u>28,192</u>

(Continued)



## WORTHINGTON ARMSTRONG VENTURE

### Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

Depreciation and amortization expense were \$3,648, \$3,276 and \$4,367 in 2008, 2007, and 2006, respectively.

#### **(6) Goodwill**

Goodwill increased (decreased) by \$(48), \$237 and \$189 during 2008, 2007, and 2006, respectively, due to foreign currency translation.

#### **(7) Fair Value of Financial Instruments**

The Company does not hold or issue financial instruments for trading purposes. The carrying amounts of cash and cash equivalents, accounts receivable, and accounts payable approximate their fair value due to the short-term maturity of these instruments. The carrying value of debt approximates fair value as the debt carries a variable interest rate.

#### **(8) Debt**

In September 2005, the Company paid off its \$50 million Term Loan and established a \$50 million revolving line of credit. In May 2007, the Company amended the line of credit facility to extend the credit agreement to May 2012 and to increase the line of credit to \$150 million. The revolving line of credit is unsecured. At December 31, 2008 and 2007, there was \$150 million and \$100 million outstanding on this line of credit, respectively. The amount outstanding bears interest (ranging from 1.97%-3.97% and 5.26%-5.7% at December 31, 2008 and 2007, respectively).

The line of credit contains certain restrictive financial covenants, including, among others, interest coverage and leverage ratios, as well as restrictions on dividends. The Company was in compliance with its covenants as of December 31, 2008 and 2007.

#### **(9) Pension Benefit Programs**

The Company contributes to the Worthington deferred profit sharing plan for eligible U.S. employees. Cost for this plan was \$1,138, \$901 and \$836 for 2008, 2007, and 2006, respectively. The Company also contributes to government-related pension programs in a number of foreign countries. The cost for these plans amounted to \$296, \$209 and \$184 for 2008, 2007, and 2006, respectively.

The Company also has a defined benefit pension plan for eligible hourly employees in its former manufacturing plant located in Malvern, Pennsylvania. This plan was curtailed in January 2004 due to the consolidation of the Company's East coast operations, which eliminated the expected future years of service for participants in the plan.

(Continued)

**WORTHINGTON ARMSTRONG VENTURE**

Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

The following table sets forth the defined benefit pension plan's benefit obligations, fair value of plan assets, and funded status at December 31, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Projected benefit obligation at beginning of year	\$ 8,703	8,999
Interest cost	511	498
Actuarial (gain) loss	111	(59)
Benefits paid	<u>(642)</u>	<u>(735)</u>
Projected benefit obligation at end of year	<u>\$ 8,683</u>	<u>8,703</u>
	<u>2008</u>	<u>2007</u>
Benefit obligation at December 31	\$ 8,683	8,703
Fair value of plan assets as of December 31	<u>5,321</u>	<u>7,636</u>
Funded status at end of year	<u>\$ (3,362)</u>	<u>(1,067)</u>

Amounts recognized in the balance sheets consist of:

Other long-term liabilities	\$ (3,362)	(1,067)
Accumulated other comprehensive loss	4,373	2,156

Amounts recognized in accumulated other comprehensive loss represent unrecognized net actuarial losses.

The components of net periodic benefit cost (benefit) are as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Interest cost	\$ 511	498	479
Expected return on plan assets	(584)	(596)	(590)
Recognized net actuarial loss	<u>209</u>	<u>203</u>	<u>241</u>
Net periodic benefit cost	<u>\$ 136</u>	<u>105</u>	<u>130</u>

The net loss for the defined benefit pension plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year is \$230.

(Continued)

## WORTHINGTON ARMSTRONG VENTURE

### Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

Weighted average assumptions used to determine benefit obligations for the years ended and as of December 31, 2008 and 2007 are as follows:

	2008	2007
<b>Weighted average assumptions for the year ended December 31:</b>		
Discount rate	5.85%	5.75%
Expected long-term rate of return on plan assets	8.00	8.00
<b>Weighted average assumptions as of December 31:</b>		
Discount rate	6.10%	5.85%
Expected long-term rate of return on plan assets	8.00	8.00

In developing the 8% expected long-term rate of return assumption, the Company considered its historical returns and reviewed asset class return expectations and long-term inflation assumptions.

The primary investment objective of the defined benefit pension plan is to achieve long-term growth of capital in excess of 8% annually, exclusive of contributions or withdrawals. This objective is to be achieved through a balanced portfolio comprised of equities, fixed income and cash investments.

Each asset class utilized by the defined benefit pension plan has a targeted percentage. The following table shows the asset allocation target and the December 31, 2008 and 2007 position:

	Target weight	Position at December 31	
		2008	2007
Equity securities	65%	64%	69%
Fixed income securities	35	31	29
Cash and equivalents	—	5	2

The Company made a \$58 contribution to the U.S. defined benefit pension plan in 2008. There were no contributions made in 2007 or 2006. The Company expects to contribute \$272 to the plan in 2009.

The benefits expected to be paid in each of the next five years and in the aggregate for the five years thereafter are shown in the following table:

<b>Expected future payments for the year ending December 31:</b>		
2009	\$	640
2010		641
2011		640
2012		638
2013		637
2014 – 2018		3,190

(Continued)

## WORTHINGTON ARMSTRONG VENTURE

### Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

The expected benefits are based on the same assumptions used to measure the Company's benefit obligation at December 31, 2008.

#### (10) Income Taxes

The Company is a general partnership in the United States and, accordingly, generally, U.S. federal and state income taxes are the responsibility of the two general partners. Therefore, no income tax provision has been recorded on U.S. income. There are no significant differences between the statutory income tax rates in foreign countries where the Company operates and the income tax provision recorded in the income statements. No deferred taxes, including withholding taxes, have been provided on the unremitted earnings of foreign subsidiaries as the Company's intention is to invest these earnings permanently.

Deferred tax balances recorded on the balance sheets relate primarily to depreciation, tax-deductible goodwill, and accrued expenses. In 2008, the provision for income tax expense (benefit) was \$5,022 comprising \$5,078 current and \$(56) deferred. In 2007, the provision for income tax expense was \$3,450 comprising \$3,292 current and \$158 deferred. In 2006, the provision for income tax expense (benefit) was \$3,754 comprising \$3,856 current and \$(102) deferred.

#### (11) Leases

The Company rents certain real estate and equipment. Several leases include options for renewal or purchase and contain clauses for payment of real estate taxes and insurance. In most cases, management expects that in the normal course of business, leases will be renewed or replaced by other leases. Rent expense during 2008, 2007, and 2006 amounted to \$2,473, \$2,470 and \$2,337, respectively.

Future minimum payments by year and in the aggregate for operating leases having noncancelable lease terms in excess of one year are as follows:

Year:	
2009	\$ 2,715
2010	2,506
2011	2,401
2012	1,942
2013	1,852
2014 Thereafter	<u>2,611</u>
Total	<u>\$ 14,027</u>

(Continued)

## WORTHINGTON ARMSTRONG VENTURE

### Notes to Consolidated Financial Statements

December 31, 2008 and 2007

(Dollar amounts in thousands)

#### (12) Accumulated Other Comprehensive Income

The balances for accumulated other comprehensive income are as follows:

	<b>2008</b>	<b>2007</b>
Foreign currency translation	\$ 4,330	8,588
Pension plan	(4,373)	(2,156)
<b>Total accumulated other comprehensive income (loss)</b>	<b>\$ (43)</b>	<b>6,432</b>

#### (13) Related Parties

Armstrong provides certain selling, promotional, and administrative processing services to the Company for which it receives reimbursement. Armstrong purchases grid products from the Company, which are then resold along with Armstrong inventory to the customer.

	<b>2008</b>	<b>2007</b>	<b>2006</b>
Services provided by Armstrong	\$ 16,143	14,961	13,706
Sales to Armstrong	98,002	87,660	75,854

No amounts were owed to Armstrong as of December 31, 2008 or 2007. Armstrong owed the Company \$2,797 and \$5,846 for purchases of product for the same periods, respectively, which are included in accounts receivable.

Worthington provides certain administrative processing services, steel processing services, and insurance-related coverages to the Company for which it receives reimbursement.

	<b>2008</b>	<b>2007</b>	<b>2006</b>
Administrative services by Worthington	\$ 474	436	23
Insurance-related coverage net premiums (refunds) by Worthington	(276)	272	683
Steel processing services by Worthington	2,215	2,076	3,646

The Company owed \$294 and \$438 to Worthington as of December 31, 2008 and 2007, respectively, which are included in accounts payable.

#### (14) Legal Proceedings

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations, or liquidity.