headlam
group plc

Europe's leading floorcovering distributor

Annual Report and Accounts **2009**

Headlam markets, supplies and distributes an extensive range of floorcovering products to independent flooring retailers and contractors throughout the UK, France, Switzerland and the Netherlands.

Our operational strategy is focused on providing our customers with an up to date comprehensive range of competitively priced floorcovering products with the support of a next day delivery.

As part of this strategy, Headlam offers its suppliers the opportunity to achieve wide market penetration backed by cost effective distribution.

In implementing this strategy, Headlam has developed a diverse and autonomous structure with 49 businesses in the UK and a further five in Continental Europe.

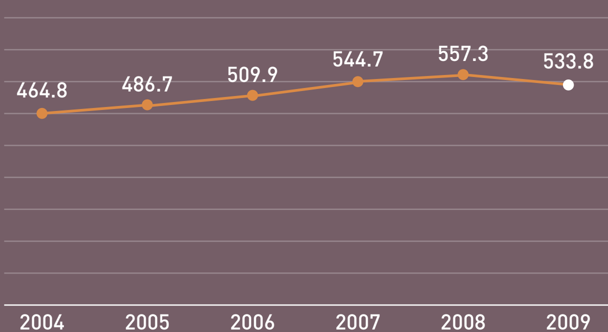
A key factor contributing to the group's success is the individuality of experienced management teams who are responsible for the market presence, development and ultimate profitability of their business.

Each business is supported by the commitment to continued investment in people, product, facilities and IT. This commitment has provided the basis for the group's growth and performance enabling it to develop into Europe's leading floorcovering distributor.

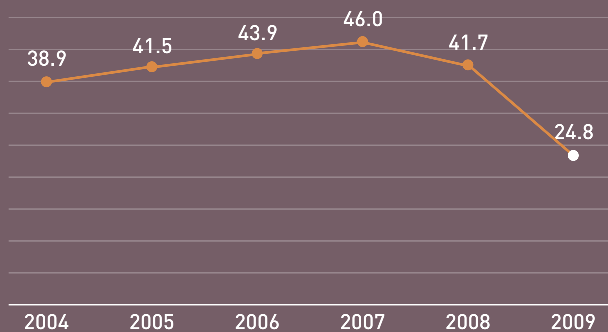
www.crucial-trading.com

www.plantationrug.co.uk

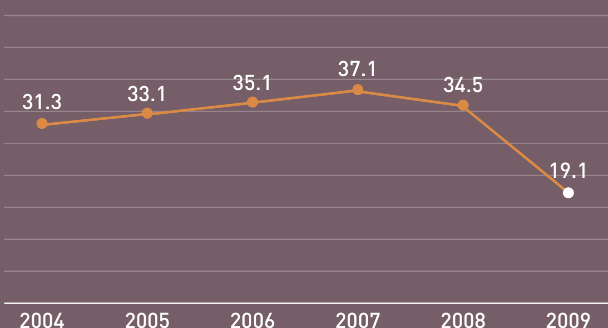
Financial Highlights



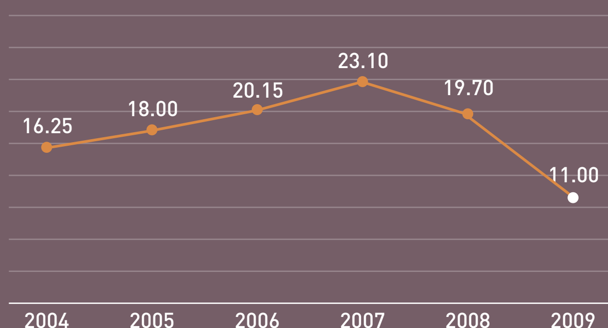
Sales (£m)



Operating Profit (£m)



Earnings Per Share (p)



Proposed Dividends (p)

Market Presence

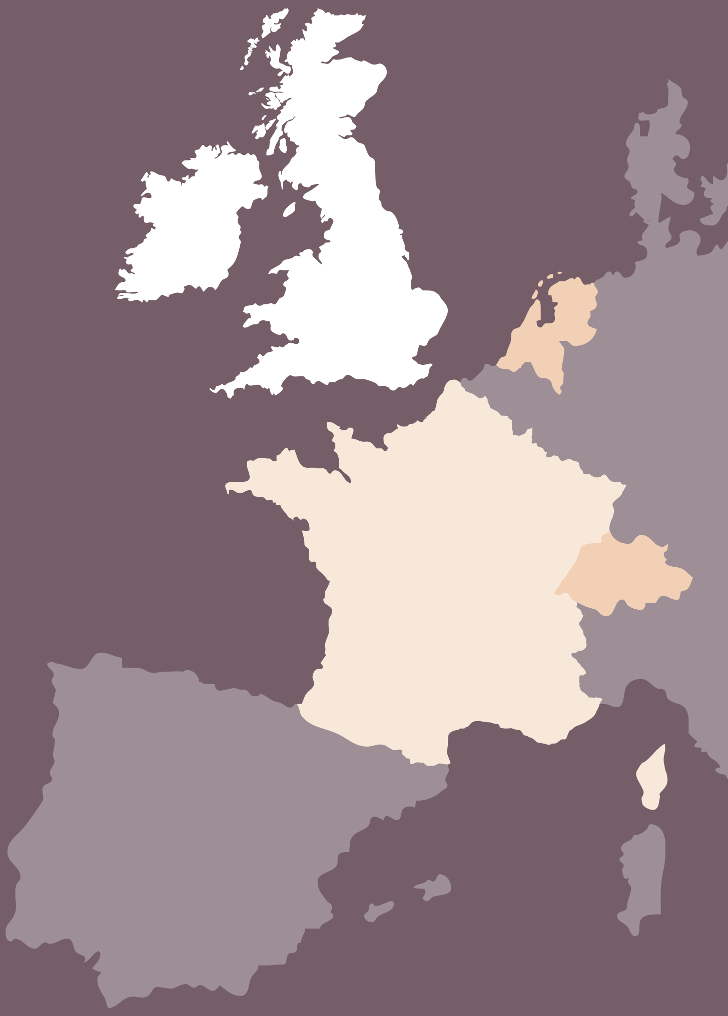
The UK operating structure is based on five business sectors each aimed at maximising market penetration and supporting different aspects of the floorcovering market.

Our Regional and National multi-product businesses provide a comprehensive residential and commercial product range and extensive geographical coverage.

The Regional commercial businesses focus on strong relationships with suppliers and a high level of localised service for their customers.

Our Residential specialist businesses supply medium to premium residential carpet on a national basis and the Commercial specialist businesses, which have a national presence, provide a range of products servicing various aspects of the commercial market.

Our business in France operates from two distribution centres and 21 service centres and the businesses in Switzerland and the Netherlands each operate from a single distribution centre. All five businesses on the Continent offer an extensive range of products providing full national coverage across their respective countries.



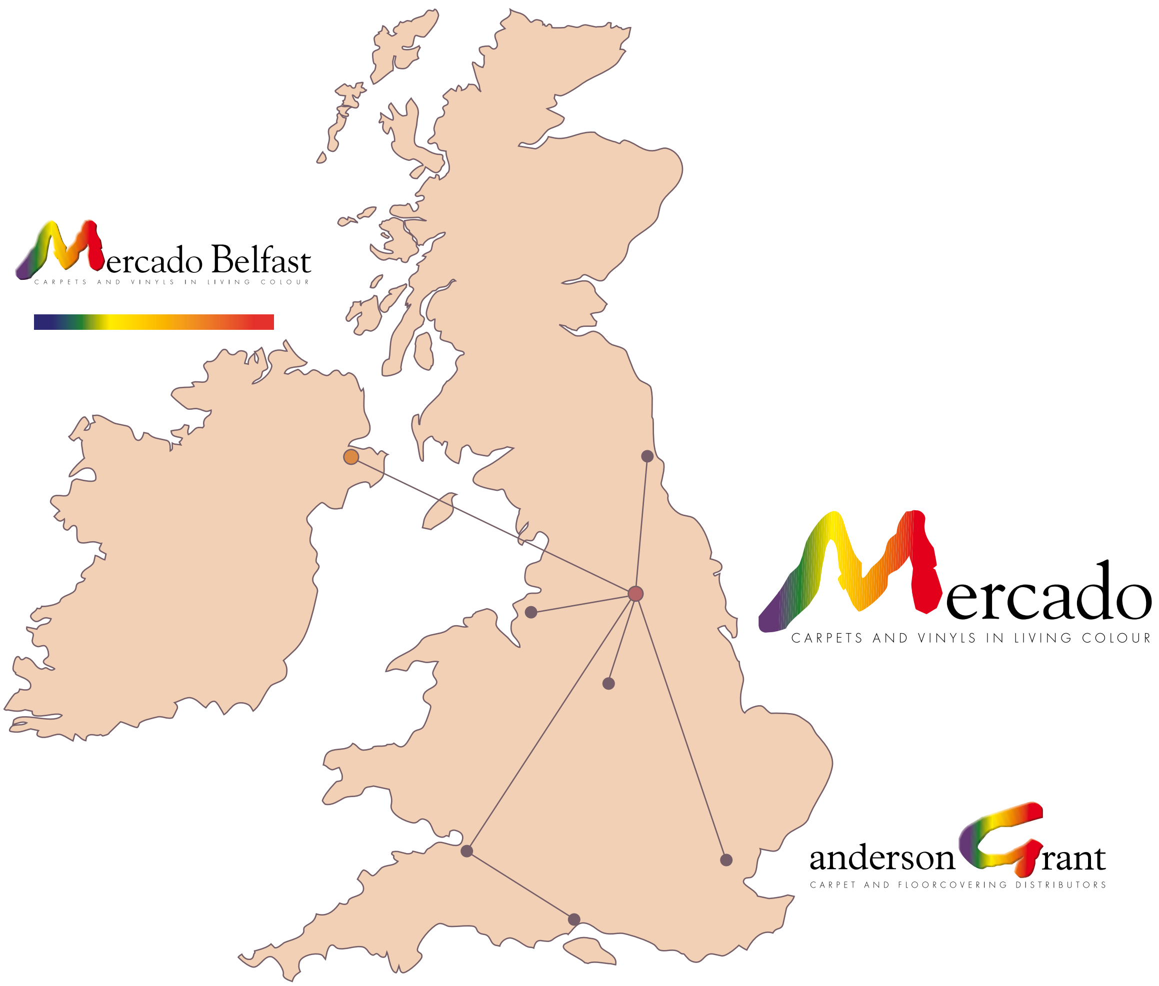
Market Presence continued

Regional Multi-product Distribution

- Distribution Centre
- Service Centre

National Multi-product Distribution

- Distribution Hub
- Distribution Centre
- Trans-shipping Location



Market Presence continued

Regional Commercial Distribution

- Distribution Centre
- Shared Distribution Centre
- Service Centre

National Multi-product Distribution

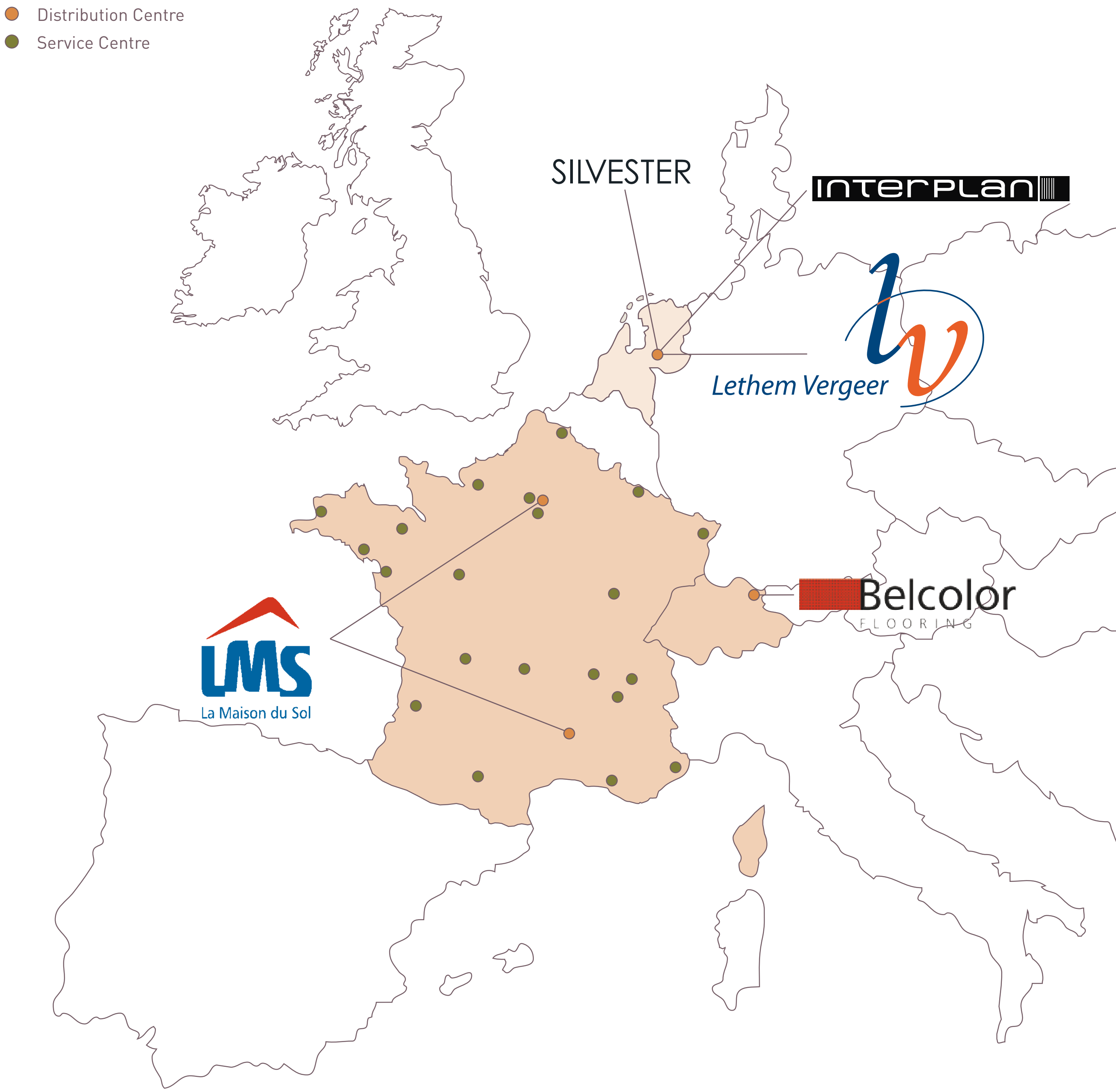
● Distribution Centre

Market Presence continued

National Commercial Specialist Products

● Distribution Centre

European Multi-product Distribution



Chairman's Statement

As anticipated, 2009 proved to be a challenging year following the downturn in market conditions that prevailed in the second half of 2008 and into the first half of 2009. More encouragingly, we experienced an improving trading trend in the second half of 2009, particularly the final quarter, as contraction in the floorcovering market appeared to cease, albeit at a level reduced on the previous year.

Total sales revenue for 2009 amounted to £533.8 million, a decline of 4.2% on the previous year. Profit before tax declined by 45.0% to £22.1 million. Notwithstanding the decline in revenue, we believe the group has out-performed the floorcovering market and by retaining our fundamental operating structure, we are well positioned to take advantage as conditions improve.

Earnings and dividend

The board has elected to maintain a dividend cover ratio in line with 2008 and is therefore recommending a final dividend of 7.3p per share. Total dividend for the year will decrease by 44.2% from 19.7p to 11.0p per share.

The final dividend, if approved by shareholders at the Annual General Meeting, will be paid on 1 July 2010, to shareholders on the register at the close of business on 4 June 2010.

Strategy

Of significant importance to the group's strategy are the autonomous activities and initiatives of our individual businesses. Whilst we implemented limited re-structuring in the autumn of 2008, we have essentially retained the same operational structure throughout 2009 in order to preserve our service levels and maintain operating capacity. Based on our trading experience towards the end of 2009, which has broadly continued into 2010, it is our intention to retain the current business structure for the foreseeable future.

The separate management teams are focused on the responsibilities specific to their business, covering activity with suppliers, product and customers, whilst complying with defined operating and financial policies. The performance measurement of our management teams and their subsequent reward is based on the achievement of their individual business objectives.

The group strategy for senior and operational management is to maintain our concentration on floorcovering distribution and enlarge our activities in the UK and Continental Europe. This will allow us to develop further the business as markets improve, through a combination of organic growth and appropriate floorcovering acquisitions as opportunities are assessed and concluded.

Operations
We believe the group has benefited significantly, in difficult markets, from the autonomous initiatives of our 49 businesses, operating from 18 principal distribution centres in the UK, each one focused on maximising activity in their target geographical areas and various product categories.

We very much appreciate the ongoing support from both our suppliers, in creating and launching new products and our customers, principally the independent flooring retailers and contractors. The ongoing success of our customers creates the opportunity to out-perform the market.

Through a constant process of development, we have launched 2,900 new products across our core residential activities of carpet, vinyl and laminate. During the year, 648,000 point of sale items, principally display stands and pattern books, were positioned into independent flooring retailers and flooring contractors by our 347 external sales people.

All three businesses in Continental Europe have made a positive contribution. Our operations in France and Switzerland performed well and in the Netherlands, progress was made despite a more challenging market.

Management and employees
Andrew Simpson, who has been instrumental in the development of Headlam, in his position as Managing Director of UK Operations since 1991, has informed the board of his intention to retire. We thank Andrew for his major contribution to the development of individual managers and the group as a whole.

David Grove, after three years as a non-executive director, has decided to step down from the board to concentrate on his other business interests. We would like to thank David for his positive contribution.

> “The core dynamics of the group are well developed and we are confident of producing a positive outcome for the year.”

With the benefit of our group structure, we have continued with our policy of internal promotion and career progression where possible. This enables employees to progress their career to sales representatives, sales and general management and in certain cases, senior management positions.

We wish to thank all of our management and employees for their contribution to the group’s performance in 2009.

Outlook
With market conditions continuing to be challenging and whilst uncertainty prevails, we have taken a prudent approach to our financial and operating plan for 2010 and set realistic growth targets for sales representatives and management teams.

The core dynamics of the group are well developed and with our autonomous management teams focused on the objectives before them, we are confident of producing a positive outcome for the year.

Graham Waldron Chairman

Chief Executive's Review

During 2009, revenue from the UK businesses collectively declined by 6.1% on a like for like basis. As reported previously, the decline in revenue was 10.7% in the first half. A generally improving performance in the second half, resulting in a like for like deficit of only 1.8%, culminated with the final quarter actually producing improved revenue of 1.0% against the corresponding period in 2008.

Various market indicators would suggest that residential and commercial floorcovering markets suffered a substantial decline during the year and therefore, we believe our result represents a solid performance.

We will continue with our strategy of concentrating on floorcovering distribution in the UK and Continental Europe. Utilising the business and management structure through which we operate, we are confident of continuing to out-perform the floorcovering market and develop our business, principally by organic growth and appropriate strategic acquisitions.

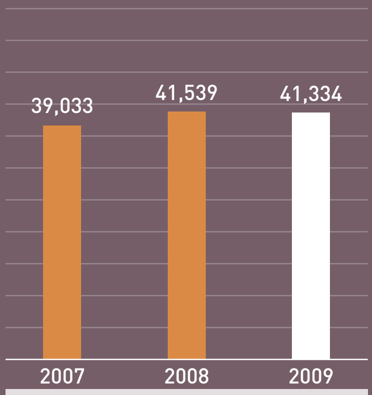
UK operations
The UK operations now incorporate 49 individual businesses, operating from 18 distribution centres and 13 service centres. The management teams of these businesses are positioned within five market sectors, dependent upon geographical focus and product offering.

Whilst we have not undertaken any significant restructuring during 2009, we have been extremely prudent with staff recruitment and therefore staff numbers in the UK, which peaked at 1,874 in 2008, have reduced from 1,729 in January 2009, to 1,661 in December 2009. Currently, the total number of staff in the UK is 1,655.

Following the restructuring in 2008 and the retention of that structure into 2009, we have ensured that our high service levels are maintained, which incorporates the ongoing launch of new products, a comprehensive stock holding and distribution infrastructure, to provide an efficient next day delivery service to our customers.

The five market sectors are:

Regional multi-product: These 20 businesses, which maximise their geographical market position by selling both residential and commercial floorcovering, now represent 53.8% of UK sales revenue.



Active Customer Accounts

National multi-product: The Mercado network of businesses, with a presence throughout England, Wales and Northern Ireland, selling residential and commercial floorcovering produced a robust performance.

Regional commercial: The 15 operations in this sector increased their revenue during the year. Through organic growth, investment and potential acquisitions, we believe this is a particular area of growth, with regard to the number of locations and revenue.

Residential specialist: The 14 businesses that represent our residential specialist activities have also increased revenue and now account for 16.5% of total UK revenue. The market presence and trade brands of our various residential specialist businesses has been strengthened through increased point of sale and an enhanced product offering, giving this business sector a particularly strong opportunity for growth over the coming years.

Commercial specialist: During the autumn of 2009, we decided to merge the sales and marketing activity of two commercial specialist businesses into the main commercial JHS brand, providing JHS with a much stronger sales and marketing platform for future growth.

Customers in the UK, who are principally independent flooring retailers and contractors, placed 4,050,577 orders during 2009

Order

Chief Executive's Review continued

Suppliers

It is encouraging that our suppliers have remained stable during this challenging period. We work very closely with our principal suppliers, both from a group perspective and through our individual management teams. This ensures an ongoing process of development and new product launches, to ensure that our customers in both the residential and commercial sectors are at the forefront of all new initiatives introduced into the UK market.

Products

Carpet remains our largest product category, accounting for 44.7% of UK revenue. We have an extremely broad base of products covering all aspects of the market and consumer taste, from base grade polypropylene to luxury woollen products.

Sales of carpet, which continue to be dominated by plain styles, produced an encouraging performance, with a revenue decline of 5.9%. This was achieved through the activity of our sales representatives positioning 2,112 new products, through 502,000 point of sale items. Our sales representatives also generated an increased proportion of sales from full rolls, which amounted to 27.5% of our carpet revenue.

UK Warehouse Storage

48

million cubic feet

Residential vinyl benefits from an ongoing improvement in production techniques, creating attractive cost-effective flooring. We were able to introduce 470 new products, marketed with 102,000 point of sale items into independent retailers.

Wood and laminate experienced the same market challenges as our other residential product categories, however, through a continual process of product launches, we were able to maintain our market position.

Rugs are an increasing presence through both independent and national retailers. The acquisition of Oriental Weavers' UK distribution activities in the spring of 2009 further enhanced our position as we develop into a leading UK supplier of both traditional and contemporary rugs.

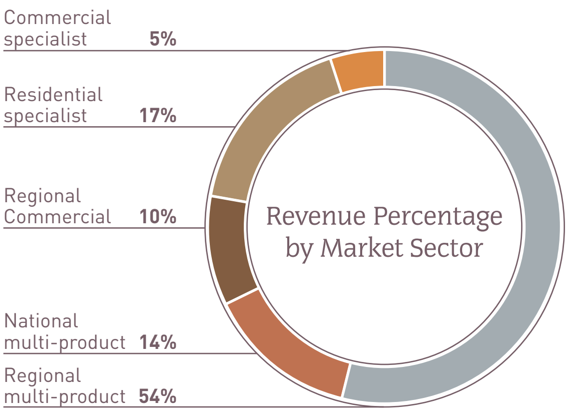
Commercial flooring activities target various aspects of the commercial flooring market through flooring contractors. Products are supplied into a variety of sectors including education, healthcare, offices and retail stores and whilst sales revenue declined by 6.3%, this again would suggest an out performance of the general commercial market.

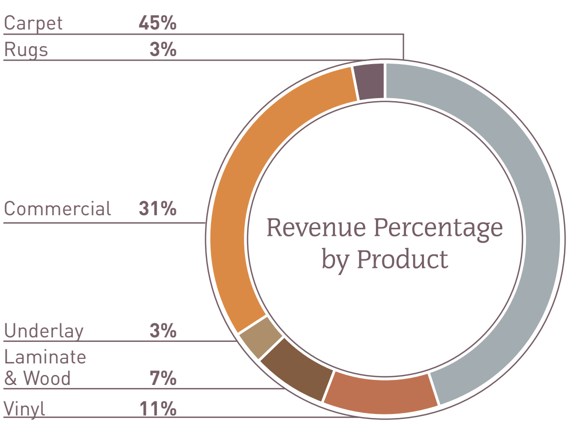
“Sales of carpet produced an encouraging performance, achieved by positioning 2,112 new products, through 502,000 point of sale items.”

Immediate order processing, comprehensive product ranges and high stock levels allow us to respond quickly to customer demand

Select

Chief Executive's Review continued





Market presence
We have increased the market presence of our various businesses, through sales representatives positioning new point of sale on a daily basis, into independent flooring retailers. This is achieved through our traditional multi-product distribution businesses and the specialist residential activities.

With the involvement and support of our suppliers, we are launching a new initiative under the Lifestyle Floors brand, to enable our multi-product distribution businesses to further strengthen their market presence within independent retailers.

Customers
The number of active accounts was stable at 41,334 (2008: 41,539.) Whilst debtor days moved marginally from 44.3 to 45.4 days, the widespread activity of our customers and payment in accordance with terms reflects the underlying strength of the independent floorcovering retailer and contractor.

UK Cut lengths

871

per hour

Continental Europe

Our businesses in France, Switzerland and the Netherlands, produced a solid performance during the year. Market conditions in France and Switzerland enabled our businesses to further develop their activities in both residential and commercial flooring.

The Netherlands proved to be a more difficult marketplace. However, with the benefit of the new 65,000 square feet distribution centre, which became operational in the spring of 2009, both Lethem Vergeer and Silvester were able to produce a satisfactory performance.

Acquisitions

We are currently assessing a number of opportunities, particularly in the UK, and would be hopeful that during the course of 2010 we will be able to complete acquisitions to enhance our market position in both residential and commercial floorcovering.

We will continue to evaluate potential acquisitions, to enlarge our core business activities in the UK and Continental Europe.

Investment in material processing and handling equipment enables us to increase efficiency and reduce waste

Cut

Investments

We are continuing with the project to relocate Faithfulls, our regional multi-product business in the south east of England, to a development site in Hadleigh, near Ipswich. We would anticipate finalising the purchase of land during the course of this year, with the construction of a 127,500 square feet purpose built freehold distribution centre completing in the summer of 2011.

We have since 2004, occupied on a leasehold basis, 50% of a distribution centre in Rochdale, from which National Carpets operate. We are currently concluding the purchase of the 110,000 square feet freehold distribution centre which will give us ownership of the total site and provide National Carpets with increased capacity and an opportunity to enlarge its activities.

With the growth of our regional commercial businesses, it is still the group's intention to increase the number of service centres in key geographical locations.

UK Deliveries

22,600

per week

Outlook
Following a more positive end to 2009, we are optimistic about a return to growth in 2010. However, market conditions, particularly in the UK, continue to be challenging, which has made normal seasonal trends and predictability difficult to establish.

Notwithstanding the current uncertainty, we believe the management and structure is in place to enable us to continue out-performing the market and take advantage of any improvement in the economy.

Tony Brewer Group Chief Executive

> "The management and structure is in place to enable us to continue out-performing the market and take advantage of any improvement in the economy."

Orders, which are received on a daily basis, are processed immediately and subject to customers requirements delivered the following day

Deliver

Financial Review

TRADING

Revenue

Group revenues declined during the year by 4.2% from £557.3 million to £533.8 million.

In the UK, like for like revenue decreased by 6.1% and revenue from the Continental European businesses, reduced on a like for like basis by 8.3%. However, group revenue has benefited from currency gains amounting to £11.6 million.

Gross margin

Gross margin, expressed as a percentage of revenue, decreased from 31.3% to 30.4%, the reduction occurring because of a change in product mix and the absence of any significant price increases during the year. The change in product mix was attributable to the higher proportion of roll sales during the year.

Inflationary pressures still remain a concern because of the continuing weakness of Sterling and in particular, the affect on cost of goods sourced from Continental Europe.

Expenses

Distribution and administration expenses, collectively representing 25.8% (2008: 23.8%) of revenue, increased by 3.5% compared with the previous year.

Distribution expenses amounting to £100.7 million (2008: £98.5 million) have increased by 2.2% compared with last year, the increase being wholly attributable to the currency effects arising from the translation of the Continental European businesses. Underlying this overall position is a decrease in expense associated with the contraction in the number of commercial vehicles and fuel which has been offset by pay increases introduced at the start of the year.

Administration expenses increased by 7.0% from £34.4 million to £36.8 million due to a combination of currency translation and the charge associated with impairment of assets held for sale. The underlying position reveals an offset with pay increases generally equating to reductions in property related expenses.

Impairment of assets held for sale

During early 2010, we disposed of two vacant properties. In both instances, the selling price was less than book value. The impairment, amounting to £1.2 million, has been recognised in the 2009 results by transferring the properties to assets held for sale at their market value and recognising the loss in the Income Statement.

We now have two vacant properties remaining in the freehold property portfolio, which are currently being marketed for disposal. However, given the limited interest, it is unlikely that these properties will be sold in the foreseeable future.

Net finance costs

Net finance costs increased by 68.2% from £1.6 million to £2.7 million as a result of a significant change in the income and expense associated with the defined benefit plan. During the year, the return on plan assets reduced from £3.9 million to £3.1 million whilst interest on the plan's obligations increased from £4.1 million to £4.2 million. The net finance costs associated with funding the group's operations were largely unchanged.

Taxation

The effective tax rate for the year was 28.0%. Going forward, we anticipate a progressive increase in the group's underlying rate, which over the medium term, is likely to rise to just over 30.0%.

Dividends

Dividend cover has been maintained at a level which is consistent with the prior year ratio of 1.7 times. Therefore, total dividends for 2009, amounting to 11.0p per share, have decreased by 44.2% on the previous year. During the year, the board has taken the opportunity to rebase the weighting between the interim and final dividend increasing the interim to approximately one third of the total dividend for the year. The board anticipate maintaining this balance for the future.

Cash flows and net funds

Cash generated from operations

Cash flows from operations before net movement in working capital, declined by 33.2% during the year from £47.1 million to £31.5 million due primarily to the decrease in profit before tax for the year.

Investment in net working capital reduced substantially compared with last year moving from a net cash outflow of £19.7 million in 2008 to a net cash inflow of £12.2 million during the year as the group rebalanced its requirements to service the reduction in revenue activity. As a result cash generated from operations increased from £27.4 million to £43.7 million.

Investment in inventories and trade receivables decreased by £6.6 million and £3.0 million respectively, and following the change in purchasing activity during the second half of 2008, which occurred because of the reduction in revenue, purchasing resumed during the year but at levels supporting the group's current need. This resulted in a cash inflow from trade and other payables amounting to £2.5 million.

Cash flows from investing and financing activities

Net cash outflows from investing activities totalled £5.8 million compared with £7.1 million during 2008. Investment in property, plant and equipment amounted to £7.3 million compared with £10.7 million for 2008. The two main areas of expenditure related to completing the Dutch property, £2.4 million, and acquiring the freehold interest, £3.1 million, of the site located in Kidderminster which was formerly occupied on a leasehold basis.

Net cash flow from financing activities moved from a cash inflow of £13.1 million during 2008 to a cash outflow of £15.2 million in 2009, the principal differences between the two years being the proceeds from borrowings amounting to £33.7 million in 2008, an absence of share buy-back activity in 2009 and a reduction in dividends paid.

Changes in net funds

Group net funds increased from £0.7 million to £9.7 million during the year as detailed in the table below

Employee benefits

During the year, the employee benefits net deficit, as measured under IAS 19, increased by £8.2 million from £14.6 million to £22.8 million. The adverse movement on the UK defined benefit pension plan was the principal cause with the deficit increasing from £12.9 million to £21.8 million as a result of a significant increase in the defined benefit obligation brought about by a decline in bond yields.

As at 31 December 2009, membership of the UK plan totalled 870 and consisted of 103 active, 460 deferred and 307 pensioners. Given the increase in the defined benefit obligation, the company has elected to offer deferred members the opportunity to transfer out of the plan. The cost of funding the offer, if all deferred members, included in the offer, elect to accept, based on the position as at 31 December 2009, would be approximately £12.0 million. This would be expected to reduce the defined benefit obligation by approximately £22.6 million from £88.3 million to £65.7 million, leading to significant reduction in the group's exposure to the funding risks associated with defined benefit pension plans.

Changes in net funds

	At 1 January 2009 £000	Cash flows £000	Translation differences £000	At 31 December 2009 £000
Cash at bank and in hand	35,193	11,102	(558)	45,737
Bank overdraft	–	(758)	–	(758)
	35,193	10,344	(558)	44,979
Debt due within one year	(4,506)	3,244	362	(900)
Debt due after one year	(30,000)	(4,396)	4	(34,392)
	687	9,192	(192)	9,687

Facilities and going concern

The group's total bank facilities amount to £80.5 million. The UK facilities of £65.0 million are comprised of £35.0 million relating to on demand facilities, which are renewed on an annual basis and a five-year term loan amounting to £30.0 million that matures in July 2012. The group's two principal UK banks have indicated that it is their intention to renew the on demand facilities for a further twelve months.

The facilities relating to the Continental European businesses amount to £15.5 million and include a facility amounting to £5.3 million, which is repayable over a ten year term ending November 2019. The remaining facilities are renewed annually. The group's banking partners in Continental Europe have also signalled their intent to provide continued support.

Having reviewed the group's resources and a range of likely trading out-turns, the directors believe they have reasonable grounds for stating that the group has adequate resources to continue in operational existence for the foreseeable future and that it is appropriate to adopt the going concern basis in preparing the group's financial statements.

Stephen Wilson Group Finance Director

Directors, Officers and Advisers

DIRECTORS

G Waldron
Chairman ❇
Graham was appointed an executive director in June 1991 becoming Chairman later that year until 31 December 1999. On the resignation of Trevor Larman on 1 June 2006 he was re-appointed Chairman. He has 57 years experience in the floorcovering industry. He is the non-executive Chairman of Tandem Group plc.

A J Brewer
Group Chief Executive ■
Tony was appointed an executive director in June 1991, becoming Managing Director of the Floorcoverings Division in January 1992, and was appointed Group Chief Executive in November 2000. He has 32 years experience in the floorcovering industry.

S G Wilson
Group Finance Director
Steve was appointed Group Finance Director in December 1991. He is the non-executive Chairman of Synergy Health plc and is a fellow of the Institute of Chartered Accountants.

R W Peters
Non-executive Director ◆ ● ■
Dick was appointed a non-executive director in December 2005. He was formerly Senior Partner for the East Midlands practice of Deloitte & Touche in Nottingham. He is a BSc in Mathematics and Statistics and is a fellow of the Institute of Chartered Accountants. He has considerable experience of auditing large companies, both UK and overseas, transactional support and project management activities. He is a director and chairman of Headlam Pension Trustees Limited.

M K O'Leary
Senior Independent Director ◆ ● ■
Mike was appointed a non-executive director in March 2006. He was formerly a director of MISYS plc and chief executive of Marlborough Stirling plc. Mike has worked in domestic and international markets and brings a wealth of general management experience to the company. He is currently a non-executive director of Psion Teklogix plc, the Stroud & Swindon Building Society and Digital Healthcare Limited, where he is Chairman.

D L Grove
Non-executive Director ◆ ● ■
David was appointed a non-executive director in October 2007. He retired from the Board of Hill & Smith Holdings PLC in December 2009 after 10 years as Chief Executive and Chairman. David is Chairman of Key Technologies PLC and a non-executive director of a number of private manufacturing, distribution and investment companies. David resigned as a non-executive director on 18 March 2010.

COMPANY SECRETARY

G M Duggan
Geoff was appointed Company Secretary in April 1998. He is a Fellow of the Institute of Chartered Secretaries and Administrators and a fellow of the Chartered Institute of Management Accountants.

EXECUTIVE MANAGEMENT

A J W Simpson
Managing Director UK Operations
Andrew joined the company in September 1991 and is the Managing Director of UK Operations. Andrew has 37 years experience in the floorcovering industry. Andrew is to retire from the business in early 2010.

G B Phillips
Finance Director Operations
Gary joined the company in June 1992 and is the Finance Director of floorcovering operations. He is an associate of the Chartered Institute of Management Accountants.

A R Judge
Managing Director, Coleshill and Tamworth businesses
Tony joined the company in May 1992 and is Managing Director of all businesses operating from the Coleshill and Tamworth distribution centres. Tony has 29 years experience in the floorcovering industry.

K R Yates
Managing Director, Mercado
Keith joined Mercado in April 1983 and was subsequently appointed its Managing Director in 1996. Keith has 27 years experience in the floorcovering industry.

◆ Audit committee
● Remuneration committee
■ Nomination committee
❇ Charities committee

ADVISERS

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Registrars
Capita Registrars
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Huddersfield HD8 0GA

Financial Calendar

Announcements

Interim Management Statement	18 May 2010
Annual General Meeting	25 June 2010
Interim results announced	27 August 2010
Interim Management Statement	18 November 2010
Full year results announced	March 2011

Dividend Dates

Final dividend for 2009, if approved, payable to qualifying shareholders on the register as at 4 June 2010	1 July 2010
Interim dividend for 2010 announced	27 August 2010
Interim dividend for 2010 payable	January 2011

Directors' Report

The directors present their annual report to shareholders on the affairs of the group and the company together with the audited financial statements and independent auditor's report, for the year ended 31 December 2009.

Principal activity
The group's activities are wholly aligned to the sales, marketing, supply and distribution of floorcovering and certain other ancillary products. The principal trading subsidiaries are listed on page 97.

Review of the business
A detailed review of the group's activities and future plans is contained within the Chairman's Statement on page 10 and the Chief Executive's Review and the Financial Review on pages 12 to 21. The information contained in these sections fulfils the requirements of the Business Review, as required by Section 417 of the Companies Act 2006 and should be treated as part of this report. The reports on Corporate Governance on pages 29 to 35 and Corporate and Social Responsibility on pages 43 to 45 are also incorporated into this report by reference. A description of the group's financial risk management objectives and policies and its exposure to price, credit liquidity and cash flow risk is contained in note 23 to the Financial Statements on page 85.

Financial results and dividends
The profit attributable to equity holders of the company for the financial year was £15.9 million as shown in the Consolidated Income Statement set out on page 47.

The directors are proposing a final dividend for the current year of 7.3p per share (2008: 14.1p), making a total dividend of 11.0p per share for the year (2008: 19.7p).The final dividend, if approved by shareholders at the Annual General Meeting ("AGM"), will be payable on 1 July 2010 to shareholders whose names appear on the register at the close of business on 4 June 2010. The associated ex-dividend date is 2 June 2010. An interim dividend of 3.7p per share (2008: 5.6p) was paid on 4 January 2010 to shareholders on the register at the close of business on 4 December 2009.

Directors and their interests
The following were directors of the company during the financial year ended 31 December 2009: Graham Waldron, Tony Brewer, Steve Wilson, Dick Peters, Mike O'Leary and David Grove, biographical details of the directors currently serving on the board being set out on page 22. No other person has acted as a director of the company during the financial year ended 31 December 2009. The company's Articles of Association ("articles") give directors power to appoint and replace directors. The articles also require directors to retire and submit themselves for election to the first AGM following appointment, that directors retire at the AGM held in the third calendar year after election or last re-election and that one third of the directors retire by rotation each year. Accordingly Graham Waldron and Dick Peters retire by rotation and being eligible, offer themselves for re-election at the forthcoming AGM.

In proposing their re-election, the board confirms to shareholders that following a formal performance evaluation, each of these individual's performance continues to be effective and they have expressed a willingness to continue in their roles.

Details of directors' remuneration and service contracts are set out on pages 39 and 40. The beneficial interests of the directors and their immediate families in the company's shares and their interests in share options are detailed on page 41.

Directors' interests in contracts
No director had, at any time during the period under review, any interests in any contract with the company or any of its subsidiaries.

Directors' indemnity
The company maintains directors and officers liability insurance and indemnity cover (as defined in sections 233 and 234 of the Companies Act 2006) which is provided for the benefit of the company's directors and officers. No indemnity is provided for the company's auditors.

Management changes
With effect from 18 March 2010, David Grove resigned his non-executive directorship to pursue other interests. The board thanks him for his contribution to the group. Additionally, the company was advised during the latter part of 2009 that Andrew Simpson was to retire, further comment in respect of which is included in the Chairman's Statement.

Principal risks and uncertainties
The group's business, results and financial condition are influenced by a range of risks and uncertainties many of which are beyond the control of the board. Whilst the following highlights some of these risks it is not intended to provide an exhaustive analysis of the risks affecting the business. For instance, there are some risks which are as yet not known and others which whilst not presently material could become a significant factor in the future.

Market demand
Approximately 94% of the group's sales are to independent retailers and flooring contractors. The activity levels within this customer base are determined by consumer demand created through residential property refurbishment or moves, new residential housing developments and a wide range of commercial refurbishment and new building projects. Periods of recession, low consumer confidence or changes in trends and preferences have the potential to affect market activity and therefore demand for products supplied by the group. However, market activity is monitored in each individual business and at group level on a daily basis which enables a rapid response to any factors adversely affecting trading. Furthermore, since the group's principal activities are supply and distribution, it has the ability to quickly respond to market changes. This, coupled with the development of broad market penetration through the establishment of a range of diverse regional, national and specialist

Directors' Report continued

businesses provides the group with a degree of resilience and protection.

Competitor risk
The group operates in four different geographical markets which generally share similar trading characteristics. Within each market, the group competes with a variety of regional and national distributors, with manufacturers selling directly to our customer base and indirectly with multiple retail chains. The group seeks to sustain its competitive position by maintaining close relationships with its supplier and customer base. Substantial and continued investment in:

- management
- an extensive product offering
- a knowledgeable sales resource
- stock availability
- IT
- efficient material handling, and
- logistics

removes the need to compete strictly on price and allows the group to enhance its overall market position through its commitment to service. The distribution competition in Continental Europe is diverse and very fragmented. The group has deliberately adopted a cautious acquisition policy in these markets, searching for opportunities that provide good growth opportunities but at sensible valuations. Given the number of opportunities it is possible that a competitor, following a more aggressive acquisition strategy in continental Europe, could challenge the group's position as Europe's leading floorcovering distributor.

Credit risk
The group trades with the majority of its customers on credit terms and therefore there is always the risk that customers are unable to pay outstanding balances. The group has standardised credit checking and debt collection procedures at each individual business. Businesses are encouraged to share credit information with other group businesses on a regular basis in order to prevent the escalation of small credit risks. All open accounts are subject to credit limits and businesses must obtain central approval for credit limits in excess of £10,000. These procedures, combined with the local knowledge of the credit control teams, not only reduce the risk of default, but also, in a number of instances, provide opportunities to assist the customer to trade out of their default position. The group does not use credit insurance since the level of default is generally low. Appropriate impairment provisions are made on a regular basis whenever the likelihood of default is high.

Infrastructure
An important element of the group's ability to service its customer base is its network of distribution and service centres. The group's policy of improvement through continued investment in new or extended facilities has been one of the principal drivers behind the group's historic growth rates. In order to support growth rates in the future, the group will continue to invest in new centres. There is a risk that future growth will be constrained if these development projects are unduly delayed through either land availability, planning consent or prohibitive building cost.

Systems
The group is highly reliant on its IT systems to deliver its operational objectives and maintain financial control. As a consequence, any prolonged IT failure has the potential to adversely affect business activity. However, each business has its own dedicated computer system and failure in one will not interrupt another. Furthermore, the group operates well defined back up procedures and has contingency plans in place to enable swift recovery from a failure of this nature.

Transport
The majority of customer orders result in deliveries within twenty four hours on vehicles operated by the group. Any interruption to this service, for example, major disruption to road networks or the prolonged reduced availability of vehicle fuel could have an adverse affect on activity.

People
The group's ability to deliver continued success is very dependant upon its people. The group is committed to providing a workplace that is safe and environmentally sound and creating opportunities for individuals to progress their careers. Recruitment, training and development are aimed at ensuring that the group has suitably skilled and qualified people to meet the operational needs of the business.

Pension
The cost of funding the group's defined benefit plans may increase due to a decline in investment returns, movement in interest rates and longer life expectancy. As a result of the triennial actuarial valuation of the UK plan, undertaken at 31 March 2008, the group agreed to make an additional payments every year until 2018, details of which are provided in note 20. The results of future scheme valuations, the next being 31 March 2011, could result in this commitment increasing.

Government legislation
The group's operations are regulated by a variety of laws, which relate, amongst others, to health and safety, the environment, employment, commercial, corporate, financial and tax. The group is committed to complying with these requirements in each of the markets in which it operates and achieves this by managing its obligations at the group level and within individual businesses. Where appropriate, the group engages the services of competent third party advisers. Changes in regulations are incorporated into the group's polices and procedures on a timely basis.

AGM
This year's AGM will be held at the group's distribution facility in Coleshill, Birmingham on Friday 25 June 2010 at 10.00am. The

notice convening this meeting is set out within this Annual Report and Accounts at page 99, along with explanatory notes regarding the resolutions that will be proposed at the meeting at pages 105 to 112.

Recommendation

The directors consider that each of the resolutions to be proposed at the AGM is in the best interests of the company and the shareholders as a whole. Accordingly, the directors unanimously recommend that all shareholders vote in favour of all resolutions, as the directors intend to do in respect of their own beneficial holdings.

Takeovers directive

The following provides the additional information required to be provided for shareholders as a result of the implementation of the Takeovers Directive into English law.

As at 31 December 2009, the company's issued share capital comprised a single class of shares referred to as ordinary shares. Details of the ordinary share capital can be found in note 22 to the financial statements which should be treated as forming part of this report.

On a show of hands at a general meeting of the company every holder of ordinary shares present in person and entitled to vote shall have one vote and, on a poll, every member present in person or by proxy and entitled to vote shall have one vote for every ordinary share held. The notice of AGM specifies deadlines for exercising voting rights and appointing a proxy or proxies to vote in relation to resolutions to be passed at the AGM. All proxy votes are counted and the numbers for, against or withheld in relation to each resolution are announced at the AGM and published on the company's website after the meeting.

There are no restrictions on the transfer of ordinary shares in the company other than:

- certain restrictions may from time to time be imposed by laws and regulations (for example, insider trading laws).
- pursuant to the Listing Rules of the Financial Services Authority whereby certain directors, officers and employees of the company require the approval of the company to deal in the company's ordinary shares.

Shareholders passed a resolution at the 2009 AGM to permit the directors to allot shares up to an aggregate nominal amount of £1,122,500. This authority will expire at the earlier of the 2010 AGM or 30 June 2010. No shares have been allotted by the company during the year.

Shareholders passed a resolution at the 2009 AGM to permit the directors to undertake market purchases of up to 12,467,000 of the company's shares. This authority will expire at the earlier of the 2010 AGM or 30 June 2010. No shares have been purchased by the company during the year.

The company is not aware of any agreements between shareholders that may result in restrictions on the transfer of securities and/or voting rights.

There are no agreements between the company and its directors or employees providing for compensation for loss of office or employment (whether through resignation, purported redundancy or otherwise) that occurs because of a takeover bid. The company's banking arrangements are terminable upon a change of control of the company.

The company's articles may only be amended by a special resolution at a general meeting of shareholders. At the 2010 AGM a special resolution will be put to shareholders proposing the adoption of new articles as described under the above AGM section and in the Notice of AGM.

Substantial shareholdings

As at the last date prior to posting the Annual Report and Accounts, in accordance with the Disclosure and Transparency Rules, the company had been notified of the following substantial interests in the share capital of the company.

Ordinary shares of 5p each

Shareholder	Number	Per cent	Nature of holding
Aberdeen Asset Management PLC	3,998,034	4.81%	Indirect
Aberforth Partners LLP	4,057,374	4.88%	Indirect
Aviva plc	5,831,244	7.02%	Direct and Indirect
AXA S.A.	4,573,109	3.39%	Direct and Indirect
Blackrock Inc	5,168,931	6.22%	Indirect
Legal & General Investment Management Limited	3,317,829	3.99%	Indirect
Liverpool Victoria Friendly Society Limited	2,644,912	3.18%	Direct
Lloyds TSB Group Plc	4,074,786	4.90%	Direct and Indirect
Schroders plc	4,119,581	4.96%	Indirect
Standard Life Investments Limited	4,111,119	4.95%	Direct and Indirect
Tweedy, Browne Company LLC	4,523,274	5.44%	Direct

Directors' Report continued

Contributions for political and charitable purposes
The group's Charities Committee considers requests for charitable donations within set criteria. During 2009, in addition to donations made to overseas charities, the group contributed charitable donations to UK charitable organisations, principally to local organisations serving the communities in which we operate, of £29,280 (2008: £9,528).

The group's policy is not to make any donations for political purposes in the UK or to donate to EU political parties or incur EU political expenditure. Accordingly neither the company nor its subsidiaries made any political donations or incurred political expenditure in the financial period under review (2008: £nil).

Financial instruments
Details of the use by the company and its subsidiaries of financial instruments can be found in note 23 to the financial statements.

Supplier payment policy
It is the group's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the company and its suppliers. The group seeks to strictly comply with these payment terms whenever it is satisfied that the supplier has provided the goods and services in accordance with the agreed terms and conditions. The payment policy has been and will continue to be developed to meet the group's specific requirements and is not based on any particular code or standard relating to payment practice. The number of creditor days of the company at 31 December 2009 was 46 days (2008: 45 days).

The environment
The group regards compliance with relevant environmental laws and the adoption of responsible standards as integral to its business operation. It is also committed to introducing measures to limit any adverse effects its business may have on the environment and will promote continuous improvement in accordance with best available techniques.

Employee involvement
The total number of employees at the end of the period was 1,989. The group recognises the value of its employees and seeks to create an energetic, dynamic and responsive environment in which to work. The company maintains a policy of employing the best candidates available in every position, regardless of gender, ethnic group or background. It places considerable importance on communications with employees which take place at many levels through the organisation on both a formal and informal level.

Employees are encouraged to own shares in the company and the group operates an HMRC Approved Savings Related Share Option Scheme (SAYE). Those employees who choose to take up the option to purchase shares in the company may enter into a savings arrangement for either a three or five year period, with the option price determined by reference to the share price at the date of grant. On exercise the shares are purchased by the employee free of income tax and national insurance, although capital gains tax rules apply.

Disabled employees
The group gives full consideration to applications for employment from disabled persons where the requirements of the job can be adequately fulfilled by handicapped or disabled persons. Where existing employees become disabled, it is the group's policy wherever practicable, to provide continuing employment under normal terms and conditions and to provide training, career development and promotion wherever appropriate. Further details of arrangements relating to employees are described in the Corporate and Social Responsibility report on pages 43 to 45.

Disclosure of information to the auditor
The directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the company's auditor is unaware, and each of the directors has taken all steps that he ought to have taken as a director to make himself aware of any relevant audit information, as defined, and to establish that the company's auditor is aware of that information.

Auditor
KPMG Audit Plc has expressed its willingness to continue in office as auditor of the company and in accordance with the provisions of section 489 of the Companies Act 2006, a resolution for its re-appointment and to authorise the directors to agree its remuneration will be proposed at the forthcoming AGM. Auditor remuneration and fees paid during the year to 31 December 2009 are set out in note 3 to the financial statements.

This directors report has been approved by the board and signed on its behalf by

Geoff Duggan
Company Secretary
19 March 2010

Statement of Directors' Responsibilities in respect of the Annual Report and Financial Statements

The directors are responsible for preparing the Annual Report and Accounts and the group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law they are required to prepare the group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and parent company and of their profit or loss for that period. In preparing each of the group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and the parent company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance statement that complies with that law and those regulations.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' Responsibility Statement in respect of the annual financial report:

The directors confirm that, to the best of their knowledge:

- The group and parent company financial statements in this report, which have been prepared in accordance with International Financial Reporting Standards as adopted by the EU (adopted IFRSs), including interpretations issued by the International Accounting Standards Board (IASB) and those sections of the Companies Act 2006 applicable to companies reporting under IFRSs as adopted in the EU, give a true and fair view of the assets, liabilities, financial position and profit of the company and group taken as a whole; and

- The management report (which comprises the Chairman's Statement, Chief Executive's Review, Financial Review and Directors' Report) includes a fair review of the development and performance of the business and the position of the company and the group taken as a whole, together with a description of the principle risks and uncertainties they face.

Signed on behalf of the board

Steve Wilson
Group Finance Director
19 March 2010

Corporate Governance

The Combined Code on Corporate Governance

The Combined Code on Corporate Governance ("the Code") issued by the Financial Reporting Council ("FRC") in June 2008 sets out guidance in the form of principles and provisions on how companies should be directed and controlled to follow good governance practice. Companies listed in the UK are required to disclose how they have applied its principles and whether they have complied with its provisions throughout the year. Companies must provide an explanation where the provisions have not been complied with.

The directors consider that the company has been in compliance with the provisions of the Code throughout the year ended 31 December 2009 and up to the date of this report.

This report sets out how the principles of the Code, which is publicly available on the FRC website www.frc.org.uk, are applied and reports on the company's compliance with the Code's provisions. The company is committed to high standards of corporate governance and supports the principles laid down in the Code.

Directors' and board effectiveness

The board of directors ("board") is collectively responsible to shareholders for the proper management and success of the group. Its role is to provide entrepreneurial leadership within a framework of prudent and effective controls which enables risk to be assessed and managed; to set strategic aims, ensure that the necessary financial and human resources are in place to meet its objectives and review management performance; to set the group's values and standards; and to ensure that its obligations to its shareholders and others are understood and met.

The roles and responsibilities of the Chairman and Group Chief Executive are clearly divided, set out in writing and periodically reviewed by the board. Whilst collectively they are responsible for the leadership of the group, the Chairman's primary responsibility is for leading the board and ensuring its effectiveness and the Group Chief Executive is responsible for implementing strategy, running the businesses in accordance with the objectives and policies agreed by the board and for the executive management of the group. The Chairman communicates frequently with the non-executive and executive directors and directors have the opportunity to discuss any issues or concerns with the Chairman at any time throughout the year. Matters that are not specifically reserved for the board and its committees under their terms of reference or for shareholders in general meeting are delegated to the Group Chief Executive.

The other significant current commitments of the Chairman are listed in his biography on page 22 and the board is satisfied that his existing commitments do not unduly restrict his availability to the group.

To help ensure the effective control of the group, the board has a schedule of items reserved for its sole consideration, most recently updated in October 2009, including but not limited to:

- group strategy, business objectives and annual plans
- major capital expenditure, acquisitions and divestments
- material agreements and major capital commitments
- changes to the group's capital structure and dividend policy
- constitution and terms of reference of the board committees, including the receiving of committee reports
- auditor remuneration and recommendations for appointment or removal of auditors
- appointments to the board and to the position of Company Secretary and approving policies relating to directors' remuneration and the severance of directors' service contracts
- ensuring that appropriate management development and succession plans are in place
- reviewing the health and safety and environmental performance of the group
- ensuring that a satisfactory dialogue takes place with shareholders
- financial reporting and controls
- approving and reviewing the group's treasury policy
- corporate governance arrangements

Further details of the board's role in relation to the group's systems of internal control and risk management are given on pages 34 and 35 . A description of the specific responsibilities delegated to the principal board committees is given on pages 31 to 33.

The effectiveness of the board is vital to the success of the group. In line with agreed procedures, using an in-house process, the board has conducted an evaluation of its own performance and that of its committees and individual directors, including the Chairman, involving the completion of a questionnaire. No actions were considered necessary as a result of the evaluations. The board intends to conduct a further evaluation of its performance during 2010 with the aim of continually improving processes, procedures and performance. The evaluation process is designed to cover board processes, the structure and capability of the board, strategic alignment, board dynamics and the skills brought to the board by each director.

Board of directors

During the year the board consisted of six members, three executive directors comprising Graham Waldron, Chairman, Tony Brewer, Group Chief Executive and Steve Wilson, Group Finance Director and three independent non-executive directors, Dick Peters, Mike O'Leary and David Grove. With effect from 18 March 2010, David Grove resigned his non-executive directorship. Mike O'Leary was the Senior Independent Director throughout the year. All of the directors bring strong judgement to the board's deliberations and the board is of sufficient size and diversity that the balance of skills and experience is considered to be appropriate for the requirements of the business. The non-executive directors are all independent of management and free from any business or other relationship, including those relationships and circumstances referred to in provision A.3.1 of the Code that could materially interfere with the exercise of independent and objective judgement. In making this determination the board has considered whether each director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could affect, the director's judgement. The board believes that it is evident from the consideration of the non-executive directors' biographies on page 22 that they are of the integrity and stature to perform their roles of independent non-executive directors. The Senior Independent Director is available to shareholders if they have concerns which are not resolved through the normal channels of the Chairman, Group Chief Executive or Group Finance Director; or for which such contact is inappropriate. The board will keep under review the size and structure of the board to ensure it is appropriate for the ongoing business.

The biographical details of the current directors are given on page 22.

The procedure for the appointment of new directors to the board is described in the section on the nominations committee below. Non-executive directors are initially appointed for a three-year term and, subject to review and re-election, can serve up to a maximum of three such terms.

All directors are subject to election by shareholders at the first AGM following their appointment by the board. Under the Articles of Association of the company, each of the directors is required to retire by rotation at least once every three years. Details of the directors retiring and seeking re-election at an AGM are given to shareholders in the Directors' Report and also in the Notice of AGM.

Board information, induction, training and professional development

All directors are equally accountable for the proper stewardship of the group's affairs. The non-executive directors have a particular responsibility to ensure that the strategies proposed by the executive directors are fully discussed and critically examined to ensure that they take proper account of the best long term interests of the shareholders, employees, customers, suppliers and the community.

To enable them to do this, the board has a forward rolling business agenda which is regularly updated to include specific topics that directors have requested for review at future meetings. The board reviews the key activities of the business receiving papers and presentations from senior management and external advisers, generally a week in advance of the meeting, to enable it to do so effectively. There is an established procedure for the preparation and review, at least annually, by the board of medium term plans and the annual budget. The board receives regular reports from the executive management covering a broad range of issues including health, safety and environmental matters, finance and operational performance, risk management, business development initiatives, special projects, legal and regulatory developments, governance and best practice guidelines that affect the group. The Company Secretary is responsible to the board, and is available to individual directors, in respect of board procedures. In conjunction with the Chairman, the Company Secretary ensures that information distributed to the board is sufficient, clear and accurate, that it is circulated in a timely manner and is appropriate to enable the board to discharge its duties.

On joining the board, a director receives a comprehensive induction pack which includes background information about the group and its directors, details of board meeting procedures, directors' responsibilities, procedures for dealing in company shares and a number of other governance-related issues. The director meets with the Group Chief Executive to be briefed on the general group strategy encompassing visits to group businesses. External training, particularly on matters relating to the role of a director and the role and responsibilities of board committees, is arranged as appropriate. Ongoing training is provided as and when necessary and may be identified in annual performance reviews or on an ad hoc basis. The suitability of external courses is kept under review by the Company Secretary. Training and development of directors in the year took various forms, including visits to group businesses with the Group Chief Executive, attendance by certain directors at courses run by professional bodies on various commercial and regulatory matters. Directors receive regular updates appropriate to the business throughout the year and the company provides resources for directors to develop and refresh their knowledge and capabilities as required. All directors are suitably qualified, trained and experienced so as to be able to participate fully in the work of the board.

To assist with the independent conduct of their function and if required in connection with their duties, the non-executive directors are able to obtain professional advice at the company's expense, and a process is in place to facilitate this. The company provides directors' and officers' insurance cover, in line with normal market practice, for the benefit of directors in respect of claims arising in the performance of their duties.

Accountability and audit

The Statement of Directors' Responsibilities in respect of the Annual Report and Financial Statements under adopted IFRS is set out on page 28. The director's confirmation that they consider it appropriate to prepare the accounts for 2009 on a going concern basis is given on page 21.

Corporate Governance continued

Board meetings and attendance

The board usually meets eight or nine times a year and normally includes at least one meeting at an operating business. During the year there are sufficient opportunities for the Chairman to meet with the non-executive directors without the executive directors being present should this be deemed appropriate. In addition, directors have frequent contact between meetings and directors visit trading locations in order to maintain close contact with the group's business.

The attendance of directors at relevant meetings of the board and of the Remuneration, Audit and Nominations committees held during 2009 was as follows:

	Board meetings	Committee meetings Remuneration	Audit	Nominations
Total number of meetings	9	3	3	1
Graham Waldron	9	*	*	*
Tony Brewer	9	*	*	1
Stephen Wilson	9	*	*	*
Dick Peters	9	3	3	1
Mike O'Leary	9	3	3	1
David Grove	9	3	3	1

* Executive directors do not attend these meetings unless invited to do so by the committee Chairman.

Board committees

The board has established Audit, Nomination and Remuneration committees to oversee and debate important issues of policy and assist in attending to its responsibilities, the terms of reference of which each comply with the provisions of the Code and are available on written request from the Company Secretary at the registered office. The audit and remuneration committees are entirely composed of independent non-executive directors.

Audit committee

The Audit committee comprised Dick Peters (Chairman), Mike O'Leary and David Grove. The board has determined that Dick Peters has recent and relevant financial experience. Only members of the committee are entitled to be present at meetings however the auditor, Chairman, Group Chief Executive and Group Finance Director attend meetings by invitation. The company does not have a formal internal audit function, considering that one is not appropriate. However detailed monthly reviews are carried out by the Finance Director for Operations and Financial Controller. The Finance Director for Operations reports to the Group Finance Director and has access to the Chairman of the committee. The committee members, all other directors and senior management have direct access to the external auditor throughout the year, to seek advice or raise any issues or concerns. The committee monitors the integrity of the company's financial statements and the effectiveness of the external audit process. It is responsible for ensuring that an appropriate relationship between the company and the external auditor is maintained, including reviewing non-audit services and fees, and makes recommendations to the board on the appointment, re-appointment or dismissal of the external auditor. It also reviews the group's systems of internal control and the processes for monitoring and evaluating the risks facing the group on an ongoing basis. The committee periodically reviews its terms of reference and its effectiveness and recommends to the board any changes required as a result of such review.

The committee has an agenda linked to events in the group's financial calendar, normally meeting at least twice a year, including meetings before the annual and interim results announcements. The committee met three times in the year, members' attendance record being given above, during which it discharged its responsibilities as set out in its terms of reference and schedule of business for the year. All of the committee members attended the meetings that they were eligible to attend. The committee has authority to investigate any matters within its terms of reference, to access resources, to call for information and to obtain external professional advice at the cost of the company.

At each meeting there is an opportunity for the external auditor to discuss matters with the committee without any executive management being present. The committee has independent access to the external auditor who has direct access to the Chairman of the committee outside formal committee meetings. The Audit committee has the specific task of keeping under review the nature and extent of non-audit services provided by the external auditor in order to ensure that objectivity and independence are maintained. The external auditor has in place processes to ensure its independence is maintained including safeguards to ensure that, where it does provide non-audit services, its independence is not compromised. It has written to the Audit committee confirming that, in its opinion, it is independent.

During the 2009 financial period, the Audit committee discharged its responsibilities by:

- reviewing the group's draft 2008 preliminary annual results announcement and financial statements and 2009 interim results statement prior to board approval, including consideration of the significant accounting judgments contained therein, and reviewing the external auditors' detailed reports thereon
- reviewing the consistency of and any changes to the group's accounting policies, the application of appropriate accounting standards and methods used to account for significant or unusual transactions.
- reviewing regularly the potential impact on the group's financial statements of certain matters such as impairment of asset values and employee benefits
- reviewing the effectiveness of the 2008 external audit process and recommending to the board, after due consideration, the re-appointment of the incumbent external auditor at the AGM
- reviewing the application of the board's policy on non-audit work performed by the group's external auditor together with the non-audit fees payable to the external auditor in 2008
- reviewing the external auditors' plan for the audit of the group's 2009 accounts, which included key areas of focus, key risks on the accounts, confirmations of auditor independence and the proposed audit fee and approving the terms of engagement for the audit
- reviewing reports from the external auditor on the group's systems of internal control in advance of the announcement of the group's results for 2008 (the internal report included a summary of and commentary on the business risks and internal control processes) and reporting to the board on the results of this review and reviewing interim updates prior to the interim results
- receiving regular updates from management on key financial control matters arising in the group
- considering the appropriateness of an internal audit function

During the year the committee reviewed the scope and programme of work to be undertaken by the external auditor, considered the independence and objectivity of services provided and reviewed the level of fees paid for those services. Whilst KPMG have been an external auditor to the group since 1991, there is a procedure in place for the audit partner to change every five years, so maintaining objectivity and independence without the need to change firms, the last such change taking place during 2008.

Resolution 5 set out in the Notice of AGM recommends that shareholders re-appoint KPMG Audit Plc as the group's auditor and resolution 6 authorises the directors to determine their remuneration.

When appointing advisers for non-audit work, the group considers the value for money, experience and objectivity required and in this respect it has used Deloitte to conduct non-audit tax work. The committee recognises that there are occasions when it is advantageous to use the external auditor to undertake non-audit services, when they are best placed to do so. The committee operates under a formal policy approved by the board to help ensure the independence and objectivity of the external auditor is not compromised. The policy states that non-audit fees paid to the principal external auditor should not exceed 250% of the audit fee, except in the case of significant events. The Chairman of the committee is required to authorise non-audit work above a pre-agreed threshold. Note 3 to the group accounts provides a breakdown of 2008 and 2009 audit and non-audit fees. In 2009, the non-audit services provided by the external auditor predominantly in respect of P11D software amounting to £2,000 was below the pre-agreed threshold.

Remuneration committee

The Remuneration committee comprises Mike O'Leary (Chairman), Dick Peters and David Grove. It met three times in the period. The committee determines, on behalf of the board, service contract terms, remuneration and benefits, including bonuses, for executive directors and senior managers. It is also responsible for the granting of share based incentive awards. Further information on the activities of the committee is given in the directors' Remuneration Report on pages 36 to 42 which should be read in conjunction with this report. The directors' Remuneration Report also describes how the principles of the Code are applied in respect of remuneration matters and includes a statement on the company's policy on directors' and senior managers' remuneration, benefits, share scheme entitlements and pension arrangements.

A resolution to approve the Remuneration Report will be proposed at the AGM.

Nominations committee

During the year the Nominations committee consisted of the non-executive directors, Mike O'Leary, Dick Peters and David Grove, and the Group Chief Executive, Tony Brewer, under the Chairmanship of Mike O'Leary. Appointments to the committee are made by the board. The committee leads the process for identifying and makes recommendations to the board on candidates for appointment as directors of the company and as Company Secretary, giving full consideration to succession

Corporate Governance continued

planning and the leadership needs of the group. It also makes recommendations to the board on the composition and Chairmanship of the Audit and Remuneration committees. It keeps under review the structure, size and composition of the board, including the balance of skills, knowledge and experience and the independence of the non-executive directors, and makes recommendations to the board with regard to any changes. The committee meets periodically when required. The Nominations committee met once in the year, as reflected in the attendance record during 2009 given above. Only members of the committee are entitled to be present at meetings but others may be invited by the committee to attend. The board has agreed the procedures to be followed by the Nominations committee in making appointments to the various positions on the board and as Company Secretary. The committee has access to such information and advice both from within the group and externally, at the cost of the company, as it deems necessary. This may include the appointment of external executive search consultants, where appropriate. No director is involved in any decisions regarding their appointment.

All non-executive directors are appointed for an initial three year term pursuant to a standard letter of appointment, which is available for viewing at the company's registered office during normal business hours or at the AGM.

The committee ensures that newly appointed directors receive a full induction and when considering the re-appointment of directors ensures that the board has an appropriate balance of skills, knowledge and experience. Items discussed by the committee during the year to enable it to discharge its duties in accordance with its terms of reference included:

- the size, structure, composition and skills of the board membership
- the proposal to re-elect Graham Waldron and Dick Peters under the retirement by rotation provisions
- the board and board committee evaluation process

The committee, in conjunction with the board, receives updates from the Group Chief Executive on succession and development planning for senior positions within the group. Changes to directors' commitments are reported to the committee as they arise and are considered on their individual merits. There were no significant changes to any of the directors' external commitments during the year.

Communication with shareholders

The company places considerable importance on communication with shareholders and engages with them on a wide range of issues. The board aims to present a balanced and understandable assessment of the group's financial position and prospects in its reporting to shareholders and this is outlined in the Financial Review. The company reports formally to shareholders twice a year when its half year and full year results are announced and an interim and a full year report is issued to shareholders.

The company has an ongoing programme of dialogue and meetings between the executive directors and institutional investors and analysts which cover strategy, trading and market conditions. The company seeks to present an accurate and objective view in a manner appropriate for the intended audience. Contact with the major shareholders is principally maintained by the Group Chief Executive and Group Finance Director. The Chairman ensures that the views of shareholders are communicated to the board as a whole.

The Group Chief Executive and Group Finance Director have met with the company's brokers during the year to ensure they are aware of the current views of major shareholders and of any material issues they may have. These reports include summaries on the market's reaction to results announcements and the subsequent meetings between management and investors. External brokers' reports on the company are circulated to all directors.

The Senior Independent Director and the other non-executive directors are invited to attend presentations to analysts and institutional shareholders, in particular the annual and interim results presentations. No specific meetings were requested by shareholders with the non-executive directors during the year.

The company's AGM provides a valuable opportunity for the board to communicate with private investors. At the meeting, the company complies with the Code as it relates to voting, the separation of resolutions and the attendance of committee chairmen. Wherever possible directors attend the AGM and shareholders are invited to ask questions during the meeting and to have the opportunity to meet with the directors following the conclusion of the formal part of the meeting. The group seeks to present an accurate, objective and balanced picture in its annual and interim reports, trading statements, results presentations and city announcements in a style and format which is appropriate to the intended audience. Copies of annual and interim reports, along with other published information and press releases, are available on the company's website at www.headlam.com. The notice of the AGM and related papers are sent to shareholders at least twenty-one clear days before the AGM and separate resolutions are proposed on each substantial issue. Shareholders at the meeting are advised as to the level of proxy votes received, including the percentage for and against each resolution together with the level of abstentions,

Corporate Governance continued

following each vote on a show of hands. In line with the Code, details of proxy voting by shareholders, including votes withheld, are made available on request and are placed on the company's website following the AGM.

Details of the 2010 AGM are set out in the Notice of AGM which forms part of these Annual Report and Accounts along with details of the facilities available for proxy votes to be cast electronically. The company offers shareholders the right to withhold their vote, if they so wish, in line with best practice.

Risk management and internal controls
The Code requires directors to review and report annually to shareholders on the effectiveness of the company's systems of internal control which include financial, operational and compliance controls and risk management. The board has overall responsibility for establishing and maintaining the group's systems of internal control and for reviewing its effectiveness whilst the implementation of internal control systems is the responsibility of management. The board continues to apply the internal control provisions of the Code through a continuous process for identifying, evaluating and managing the significant risks the group faces. This process has been in place throughout the year and up to the date of approval of this report, and the group has been in compliance with the provisions set out in section 1 of the Code. This includes consideration of corporate social responsibility matters.

The systems are designed to meet the group's particular needs and to manage, rather than eliminate, the risks to which the businesses are exposed. By their nature, they provide only reasonable and not absolute assurance against material misstatement or loss. The board considers that the measures taken, including physical controls, segregation of duties and reviews by management, provide sufficient and objective assurance.

During the year the board maintained its process of hierarchical reporting and review in order to evaluate the effectiveness of the group's systems of financial and non-financial controls. The group has developed a comprehensive series of operating and financial control procedures which are applied at all businesses and the group finance team performs monthly reviews to verify that the businesses are complying with the prescribed operating and financial control procedures. In addition, the board reviews risk management arrangements. Furthermore, the Audit committee receives reports from the external auditor on matters identified in the course of its statutory audit work.

These procedures provide a documented and auditable trail of accountability, the results of which are periodically reviewed by management for completeness and accuracy. These procedures allow for successive assurances to be given at increasingly higher levels of management through to the board. Planned corrective actions are monitored for timely completion. Having reviewed its effectiveness, the directors are not aware of anything in the group's systems of control during the period covered by this Annual Report and Accounts which could render them ineffective. There were no changes in the group's internal controls or financial reporting that have materially affected, or are reasonably likely to affect, the group's systems of internal control.

The group operates a comprehensive planning system, including detailed reviews at all subsidiary undertakings, together with formal reviews and approval of annual plans by the board. Actual performance is reported on a monthly basis measured against plan and prior year including a detailed explanation of major variances and on a daily basis, sales, margin and cash flow, measured against plan and prior year are reported. The company and its subsidiary undertakings have implemented control procedures designed to ensure complete and accurate accounting for financial transactions and to limit the potential exposure to fraud. The group has clearly defined guidelines for capital expenditure and investment appraisal. These include annual plans, detailed appraisal and review procedures, levels of authority and due diligence requirements when businesses are acquired. Any acquisition or disposal of a business needs formal board approval. The board reports that full procedures are in place to achieve compliance with the internal control aspects of the Code for the next financial period.

The output of these reviews form an important element of management reporting and a process is in place for monitoring the achievement of action plans together with the identification of new and emerging risks. An ongoing process of risk management and internal control in accordance with the Code has been in place for the financial year under review and up to the date of this report. The group views the careful management of risk as a key managerial activity in delivering business opportunities. The ethos of the group, delegation of responsibility and other control procedures together with accounting policies and procedures are communicated through the group and laid out in the group procedures manual, which is periodically updated, and the employee handbook.

Corporate Governance continued

The objective of the group's risk management processes is to ensure sustainable development throughout the conduct of its business in a way which:

- satisfies its customers
- maintains proper relationships with suppliers and contractors
- protects against losses from unforeseen causes
- provides a safe and healthy workplace
- develops environmentally friendly processes
- minimises the cost and consumption of increasingly scarce resources
- prevents pollution and waste
- maintains a positive relationship with the communities in which it does business

A high standard of health and safety management is promoted at all levels within the group. The group's health and safety approach is supported by training programmes at operating businesses, group health and safety rules and monitoring and auditing to promote a high level of awareness and commitment. Individual businesses are assessed on a periodic basis, and remedial solutions implemented where necessary. Line management retain the responsibility for completion of action plans with progress being monitored and reported.

The Audit committee meets at least twice a year and in accordance with its terms of reference, reviews the effectiveness of the group's systems of internal control. In accordance with the Code the board has undertaken an assessment of the need for a group internal audit function. The board considers that the control systems and procedures undertaken by the group are adequately performed by management and therefore does not currently propose to introduce a group internal audit function but will keep the matter under review.

The integrity and competence of personnel is assessed during the recruitment process and monitored throughout employment. Ethical standards expected of personnel are laid out in the group procedures manual and in the employee handbook.

The system for monitoring risks is continuous and an ongoing process throughout the year. Principal risks and uncertainties are set out on pages 24 and 25 of the Directors' Report.

This process has identified a number of risks where action plans have been developed to eliminate, minimise or mitigate these risks (including the use of insurance where appropriate).The board has not identified or been advised of any significant failings or weaknesses where action has not been taken which might have a material impact on the business.

The Corporate Governance Report and the Audit Committee Report contained in it have been approved by the board and are signed on its behalf by

Geoff Duggan
Company Secretary
19 March 2010

Remuneration Report

Introduction

This report, which has been approved by the board, has been prepared in accordance with the requirements of the Directors' Remuneration Report Regulations 2002, the Listing Rules of the Financial Services Authority and the relevant schedules of the Companies Acts.

The purpose of this report is to inform shareholders how the company has applied the principles of the Combined Code on Corporate Governance that relate to directors' remuneration during the period. The report describes the group's remuneration policy as it applies to directors and senior executives and provides detailed disclosures in relation to directors' remuneration in current and prior years and so far as practicable, for subsequent years as well.

The report is divided into two parts. The first part, which is not required to be audited, details the role of the committee and commentary on remuneration policy. The second part contains the remuneration review detailing directors' and former directors' emoluments, share awards and options and pension arrangements that have been audited in accordance with the relevant statutory requirements.

In accordance with the Companies Act 2006, a resolution will be submitted to the forthcoming AGM, to be held on Friday 25 June 2010, seeking shareholder approval for the directors' Remuneration Report.

Composition and role of the Remuneration committee

The Remuneration committee is appointed by the board and comprised three non-executive directors, Mike O'Leary (Chairman), Dick Peters and David Grove during the year under review. All the committee members served throughout both the period under review and the prior period. The three committee members have no personal financial interest, other than as shareholders, in matters to be decided, no potential conflicts of interest and, as independent non-executive directors, no day to day involvement in running the business. The biographical details and qualifications for each of the committee members are shown on page 22. Details of members attendance at the meetings of this committee, which meets not less than three times a year, are shown in the report on Corporate Governance on page 31 and directors' shareholdings are shown later in this report on page 39. The Group Chief Executive, by invitation, may attend meetings of the committee in an advisory capacity. Meetings are attended by the Company Secretary who acts as secretary to the committee. Nobody attends any part of a meeting at which their own remuneration is discussed. The remuneration of the non-executive directors is the responsibility of the other board members.

The committee is responsible for setting the framework and policy for the remuneration of the executive directors which it reviews annually for appropriateness and relevance. It is also responsible for determining the specific elements of the executive directors' and executive managements' remuneration, performance targets, their contractual terms and compensation arrangements. This is to ensure that on termination, contractual terms and payments are fair both to the company and to the individual so that failure is not rewarded and that the duty to mitigate loss is recognised. In addition, the committee oversees any major changes in employee benefit structures throughout the group.

The terms of reference of the committee are available from the company on request. In setting policy and compensation levels, the committee has due regard to the Combined Code. The committee has access to advice provided by the Group Chief Executive, Company Secretary and external consultants, agreeing the terms of reference of any remuneration consultants it may appoint. During 2009 the committee sought information from a wide variety of published sources, and members attended seminars on the subject, to assist in the formulation of the committee's recommendations and in respect of retirement benefits and executive remuneration. Similar to prior year, the committee did not make any specific appointments in sourcing such information.

Remuneration policy

The group's remuneration policy seeks to ensure that the remuneration of executive directors and executive management is sufficiently competitive to enable the group to retain and motivate existing directors and attract high quality individuals in the future. It has the objective of providing remuneration packages that are challenging and competitive in both commercial and human terms and facilitate effective succession planning.

In setting its policies, the committee has regard to several factors including the benefits arrangements which apply below senior management level and competitor benchmarking.

The committee aims to achieve a balanced package for each executive director, reviewing executive directors' remuneration annually. The company believes that in order to meet its remuneration objectives, the remuneration of executive directors should comprise a balance between fixed and variable performance related pay elements with a significant proportion of the potential remuneration dependent on the attainment of performance objectives, both through the annual bonus scheme and through participation in share incentive schemes.

The committee constantly reviews remuneration policy to ensure that it is sufficiently flexible to take account of future changes in business operations and environment and recognises key developments in remuneration practice and alignment to shareholder interests. Participation in share incentive schemes is designed to align the interests of executive directors and other senior executives with the longer-term interests of shareholders by rewarding them for delivering increased shareholder value which provide opportunities to build shareholdings in the company.

Remuneration Report continued

The Remuneration committee, through the executive directors and Company Secretary, seeks the views of the company's principal shareholders as necessary. In determining the level of base salaries and the annual performance related bonus scheme, the committee takes into consideration the potential maximum remuneration that executives could receive.

In implementing this policy, the Remuneration committee takes account of information and surveys from internal and independent sources and the remuneration paid for comparable positions in other companies. It reviews data and surveys provided by a wide variety of published sources with reference to the scale and composition of the total remuneration packages payable to people with like responsibilities, qualifications, skills and experience in businesses of similar size and structure. In setting the remuneration of the directors and executive management, the committee takes into account the economic environment and financial performance of the group, along with pay and employment conditions of employees elsewhere in the group.

The group's remuneration policy in respect of non-executive directors is to pay annual fees, which reflect the responsibilities and duties placed upon them, whilst also having regard to market practice.

The total emoluments of the executive directors are disclosed on page 40.

No director is involved in the determination of, or votes on any matter relating to their remuneration.

For the financial year 2010 the committee has approved a decision to increase the pay of UK employees by an average 1.5% except that in exceptional circumstances pay increases may be provided to individuals whose base salary is behind the market, for example, due to promotion, or to those individuals who are performing above expectation. This policy has not been applied to the directors and other executive management whose pay was not increased in 2010.

The committee is satisfied that the incentive structure for executive management does not raise governance risks by inadvertently motivating irresponsible or reckless behaviour.

Components of remuneration

Base salaries

The committee reviews base salary, which is the only element of remuneration that is pensionable, annually with any change taking effect from 1 January. As a general policy, base salaries reflect the committee's assessment of the appropriate market rate for comparable positions and levels of responsibility and the individual executive's experience, performance and value to the business. The committee also assesses pay and employment conditions of employees of the group when determining the executive directors' remuneration.

The base salary of the executive directors remained unchanged in 2009 and will continue to do so for 2010. The base salary of executive management remained unchanged in 2010.

Annual performance bonus

The committee reviews the annual performance related bonus scheme to ensure that it remains competitive in the marketplace and continues to offer an incentive to the executive directors and executive management. The scheme focuses on annual objectives and links individual performance with business financial targets. The financial targets are calculated by reference to the extent to which the group's operating profit meets the planned target. The committee establishes the objectives that must be attained for each financial year if a bonus is to be paid.

When awarding the bonus the committee takes account of the relative success of the group's performance and the extent to which strategic objectives are being attained. The performance related scheme for 2009, as reported last year, provided for a bonus award of 77% of base salary on achievement of financial target with a maximum of 150% of base salary payable for over achievement of performance related targets.

For 2009, the performance target was met and accordingly performance-related bonuses were awarded to the executive directors and executive management. The performance related components of remuneration for executive directors and executive management are paid in March following the completion of the annual audit. Details of the payments to directors are included in the directors' remuneration for the year on page 40.

The performance related scheme for 2010 is similar to that applicable to 2009 in that it provides for a bonus award of 75% of base salary on achievement of financial target with a maximum of 150% of base salary payable for over achievement of performance related targets. In the event of under performance of performance target no bonus will be awarded. Furthermore, the committee will not use discretion to make bonus awards for under performance.

Share incentive arrangements

The committee is keen to encourage directors and key employees to build up or increase their shareholdings in the company, so aligning their interests with the company's shareholders. The committee recognises the importance of share incentives in recruiting and retaining directors and key employees on whose performance the success of the company depends.

At the 2008 AGM shareholders authorised the adoption of a new HMRC approved discretionary share option scheme, the Headlam Group Approved Executive Share Option Scheme 2008 and a new non-HMRC approved discretionary share option scheme, the Headlam Group Unapproved Executive Share Option Scheme 2008 (together the "New Share Option Schemes"), which replaced the Headlam Group Approved Executive Share Option Scheme

Remuneration Report continued

1998 and the Headlam Group Unapproved Executive Share Option Scheme 1998 that expired in 2008 (together the "1998 Share Option Schemes"). Shareholders also authorised the adoption of the Headlam Group Performance Share Plan 2008 (the "PSP") and the Headlam Group Co-Investment Plan 2008 (the "CIP").

The committee has not yet implemented either of the PSP or the CIP.

A summary of the main terms of the 1998 Share Option Schemes, the New Share Option Schemes, the PSP and the CIP is set out below.

The 1998 approved scheme is a standard HMRC approved share option scheme under which a participant receives a right to acquire shares at a price equal to the market value of the shares at the grant date which will normally vest after three years, subject generally to continued employment and achievement of performance targets. No new options can be granted under this scheme following its expiry in 2008, however current options remain capable of exercise until their normal lapse date.

The 1998 unapproved scheme is a non-HMRC approved share option scheme under which a participant receives a right to acquire shares at a price equal to the market value of the shares at the grant date which will normally vest after three years, subject generally to continued employment and achievement of performance targets. Prior to its expiry in 2008, the unapproved scheme would have allowed the committee to grant awards in excess of the levels permitted by relevant tax legislation for the purposes of the 1998 approved scheme, although such awards would not have been tax-efficient. No new options can be granted under this scheme following its expiry however current options remain capable of exercise until their normal lapse date.

The 2008 approved scheme is a standard HMRC approved share option scheme under which a participant receives a right to acquire shares at a price equal to the market value of the shares at the grant date which will normally vest after three years, subject generally to continued employment and achievement of performance targets.

The 2008 unapproved scheme is a non-HMRC approved share option scheme under which a participant receives a right to acquire shares at a price equal to the market value of the shares at the grant date which will normally vest after three years, subject generally to continued employment and achievement of performance targets. The 2008 unapproved scheme allows the committee to grant awards in excess of the levels permitted by relevant tax legislation for the purposes of the 2008 approved scheme, although such awards will not be tax-efficient.

The PSP is a discretionary non-HMRC approved plan under which a participant receives a right to acquire shares for no cost which will normally vest after three years, subject generally to continued employment and the achievement of performance targets.

The CIP is a discretionary non-HMRC approved plan under which a participant invests the whole or part of any annual bonus in ordinary shares of the company and receives a right to acquire matching shares for no cost which will normally vest after three years, subject generally to continued employment and the achievement of performance targets.

The performance targets for options granted under the 1998 Share Option Schemes are based on the extent to which growth in the group's earnings per share ("EPS") exceeds growth in the Retail Prices Index ("RPI") over a three-year performance period, EPS being calculated as fully diluted earnings per share. In respect of the approved scheme EPS growth must exceed RPI growth by 3% pa or more over the three year performance period. In respect of the unapproved scheme, for options up to one times eligible earnings, EPS growth must exceed RPI growth by 3% pa or more over the three year performance period and by 5% or more over the three year performance period for options granted of between one times and two times eligible earnings. The committee felt that these performance conditions were appropriate at the time the options were granted.

Details of subsisting share options and shares issued under the various schemes summarised above are set out on page 41.

No new executive share options were granted in 2009, the most recent grant of options made under the 1998 Option Schemes being in 2005.

Retirement benefits
The executive directors currently participate in the Headlam Group Staff Retirement Benefits Scheme, the defined benefit plan operated by the group, on a non-contributory basis. Details regarding the executive directors' participation in the defined benefit pension plan are given on page 42.

Other employment benefits
Executive directors receive taxable benefits including a company car, private fuel, lump sum life assurance for death-in-service cover and non-contributory private medical insurance, which provides benefits similar to those applicable in comparable companies. They are also eligible to participate in the company's Inland Revenue-approved sharesave scheme which is open to all eligible employees on the same basis, providing a long-term savings and investment opportunity. The exercise of options under the sharesave scheme is not subject to the satisfaction of performance conditions as this is an all employee arrangement.

Remuneration Report continued

Service contracts

The current policy is for executive directors' service contract notice periods to be normally no longer than twelve months. The service contracts of the executive directors' have no fixed term but provide that either the director or the company may terminate the employment by giving twelve months' written notice and that the company may pay compensation in lieu of notice. The company recognises however that it may be necessary in the case of new executive appointments to offer an initial longer notice period, which would subsequently reduce to one year after the expiry of that period. All future appointments to the board will comply with this requirement.

Service agreements contain neither a liquidated damages nor a change of control clause. It is the company's policy to ensure that any payments made to a director in the event of the early termination of a service agreement reflect the circumstances giving rise to termination and, where considered appropriate, the obligation of the outgoing director to mitigate his loss. Accordingly, consideration is given to making compensation payments in instalments and is conditional on the leaver's employment and earnings status. The service agreements of the executive directors who served during the financial period were entered into on 11 October 2005.

The Chairman does not hold a service contract and does not participate in the company's executive share schemes, incentive plans or pension schemes. Additionally, he is not a member of the various committees of the board.

The service agreements of the continuing directors are available for inspection at the registered office of the company during normal business hours on each business day.

External appointments of executive directors

The board believes that experience of other companies' practices and challenges is valuable both for the personal development of its executive directors and for the company. It is therefore the company's policy to allow each executive director to accept one non-executive directorship of another company, although the board retains the discretion to vary this policy. Fees received by executive directors in respect of external non-executive appointments are retained by the individual director. In 2009 Graham Waldron and Steve Wilson received fees of £50,000 and £44,000 respectively.

Non-executive directors

The non-executive directors do not have service agreements but instead are appointed for an initial period of three years by letter of appointment which is terminable by either party subject to one month's notice, for which no compensation is payable. At the end of the initial period, the company discusses with the non-executive director whether they wish to renew their appointment and whether it is in the best interests of the company for their appointment to be renewed. Such renewal would normally be for a further period of three years (subject to termination as aforesaid). Non-executive directors are typically expected to serve two three-year terms, although the board may invite them to serve for an additional period. All appointments and subsequent re-appointment is subject to approval by shareholders.

Non-executive directors' fees are reviewed by the board annually by reference to prevailing market conditions and at a level which will attract individuals with the necessary experience and ability to make a positive contribution to the group's affairs. The annual fees were reviewed with effect from 1 January and remained unchanged at £35,000, with an additional £5,000 being paid to the respective chairmen of the Audit and Remuneration committees. Non-executive directors are not involved in any discussion or decision about their own remuneration nor do they participate in any of the company's share schemes, incentive plans or pension schemes. The aggregate limit for fees paid to non-executive directors is laid down in the articles. Mike O'Leary has been designated Senior Independent Director for which he receives no additional fees.

Non-executive directors' appointment dates are shown on page 22.

Directors' interests in shares

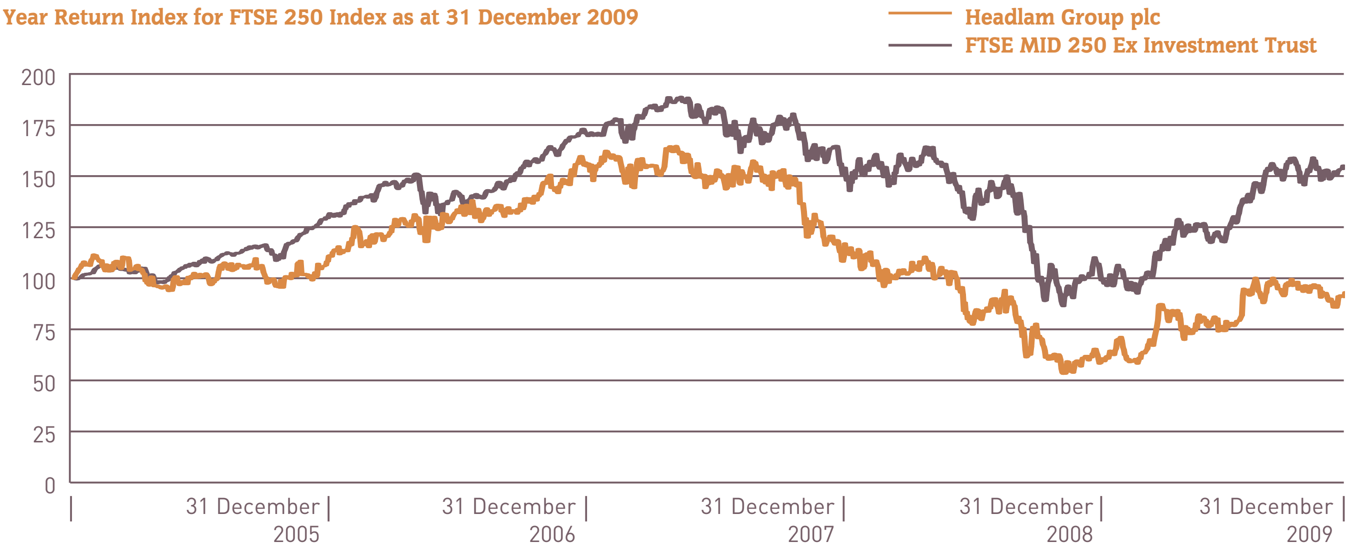
In accordance with Listing Rule 9.8.6R, the two tables set out below show the beneficial interests of the directors, and their connected persons, who held office at the end of the year in the ordinary shares of the company and the interests in the company's share schemes.

	Shareholdings at 31 December 2009	Shareholdings at 31 December 2008
Executive Directors		
Graham Waldron	360,638	360,638
Tony Brewer	519,942	519,942
Steve Wilson	400,770	400,770
Non-executive Directors		
Dick Peters	5,000	5,000
David Grove	30,000	30,000
Mike O'Leary	–	–

The interests in shares of the directors were unchanged at 19 March 2010 from those at 31 December 2009. It is the company's policy that executive directors are required to hold ordinary shares of 5p in the company equivalent in value to once time's base salary, newly appointed directors being expected to build their holding over a five year period.

Remuneration Report *continued*

5 Year Return Index for FTSE 250 Index as at 31 December 2009



Source: Thomson Financial

Performance graph

The above graph has been included to meet the requirements of Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008. It shows the group's performance on a holding of £100 in the company's shares for the five year period to 31 December 2009 measured by total shareholder return ("TSR"), compared with the performance of the FTSE 250 Excluding Investment Trusts index also measured by TSR, which is defined as share price growth, plus re-invested dividends. The FTSE Excluding Investment Trusts 250 index has been chosen because it provides a basis for comparison against companies in a relevant broad based equity index in which the group has predominantly over a number of years been a constituent member. The FTSE SmallCap Index, of which the company is currently a constituent member, is believed to be a less meaningful index for comparison purposes. The TSR indices used in the chart have been calculated in accordance with the Directors Remuneration Report Regulations 2002 relative to a base date at the end of December 2004. The other points plotted are the values at intervening financial year ends.

Audited information

The Remuneration Report from page 36 to page 40 up to this statement has not been audited. From this point until the end of the report on page 42 the disclosures have been audited by the company's auditor, KPMG.

Directors' emoluments

The emoluments of the directors for their services as directors of the group for the year ended 31 December 2009 were:

	Salary and fees		Benefits		Performance related pay		Total	
	2009 £000	2008 £000	**2009 £000**	2008 £000	**2009 £000**	2008 £000	**2009 £000**	2008 £000
Executive directors								
Tony Brewer	**520**	520	**35**	36	**392**	168	**947**	724
Steve Wilson	**376**	376	**28**	39	**291**	125	**695**	540
Graham Waldron	**115**	115	**26**	21	**–**	–	**141**	136
Non-executive directors								
David Grove	**35**	35	**–**	–	**–**	–	**35**	35
Mike O'Leary	**40**	40	**–**	–	**–**	–	**40**	40
Dick Peters	**40**	40	**–**	–	**–**	–	**40**	40
	1,126	1,126	**89**	96	**683**	293	**1,898**	1,515

Remuneration Report continued

Benefits are in respect of all taxable benefits arising from employment by the company including the provision of a company car, private fuel, life assurance cover and private medical insurance. Pension benefits and gains made by executive directors in respect of share options are excluded from the table above. The aggregate amount of gains made by executive directors on the exercise of share options was £nil (2008: £33,973).

Directors' interests in share option schemes

Details of options held by executive directors are set out below, a description of which is given on pages 37 and 38:

	Options held at 1 January 2009	Options granted during the year	Options cancelled during the year	Options exercised during the year	**Options held at 31 December 2009**	Exercise price (pence)	Date from which exercisable	Expiry date
Tony Brewer								
1998 USOS (i)	342,858	–	–	–	**342,858**	420.00	Aug 2008	Aug 2012
1998 ESOS (ii)	7,142	–	–	–	**7,142**	420.00	Aug 2008	Aug 2015
Sharesave (iii)	5,367	–	5,367	–	**–**	303.20	Jul 2013	Jan 2014
Sharesave (iii)	–	7,043	–	–	**7,043**	222.20	Jul 2014	Jan 2015
Steve Wilson								
1998 USOS (i)	242,858	–	–	–	**242,858**	420.00	Aug 2008	Aug 2012
1998 ESOS (ii)	7,142	–	–	–	**7,142**	420.00	Aug 2008	Aug 2015
Sharesave (iii)	5,367	–	5,367	–	**–**	303.20	Jul 2013	Jan 2014
Sharesave (iii)	–	7,043	–	–	**7,043**	222.20	Jul 2014	Jan 2015
Graham Waldron								
Sharesave (iii)	3,100	–	3,100	–	**–**	303.20	Jul 2011	Jan 2012
Sharesave (iii)	–	4,117	–	–	**4,117**	222.20	Jul 2012	Jan 2013

(i) Headlam Group Unapproved Executive Share Option Scheme 1998 (1998 USOS)
Details of the operation of the scheme including the performance conditions attaching to options are provided on page 38.

(ii) Headlam Group Approved Executive Share Option Scheme 1998 (1998 ESOS)
Details of the operation of the scheme including the performance conditions attaching to options are provided on page 38.

(iii) Headlam Group Sharesave Scheme 2002 (Sharesave)
The company operates an Inland Revenue-approved all-employee savings-related share option scheme in the UK. The scheme is designed to provide a long-term savings and investment opportunity for employees and is described on page 38.

On 19 May 2009, the company granted options under its savings related share option scheme for terms of between three and five years at an option price of 222.20 pence per share.

The mid-market ordinary share price range during the year was 200.00 pence to 327.00 pence with an average price of 268.78 pence. The mid market closing price of a Headlam Group plc ordinary share on 31 December 2009, the last trading day of the financial period, was 300.25 pence.

Remuneration Report *continued*

Pension benefits

Tony Brewer and Steve Wilson participate in the group's defined benefit pension scheme which provides benefits at a normal retirement age of fifty five based upon pensionable service. The maximum pension payable under the scheme is equivalent to an amount that would not result in any additional tax charge being payable under HM Revenue & Customs' rules. There are lump sum death-in-service benefits and pension provisions for members' dependents. Benefit accrual in respect of Steve Wilson ceased on 20 August 2009 on reaching normal retirement age.

Details of executive directors' pension benefits for the year ended 31 December 2009 are shown below:

	Increase in accrued pension during the year £000pa	Transfer value of increase £000	Accumulated accrued pension at 31 December 2009 £000pa	Change in accrued pension over the year £000pa	Accumulated 31 December 2008 £000pa
Tony Brewer	4	88	68	8	60
Steve Wilson	2	46	81	4	77

The increase in accrued pension entitlement is the difference between the accrued benefit at the year end and that at the previous year end. Transfer values have been calculated on the Trustees' cash equivalent transfer value basis. The increase in the transfer value is the increase in the value of accrued benefits during the year. The transfer value of the increase in accrued benefits, required by the listing rules, discloses the current value of the increase in accrued benefits that the director has earned in the period, whereas the change in the transfer value, required by the Companies Act, discloses the absolute increase or decrease in the transfer value and includes the change in value of the accrued benefits that result from market volatility affecting the transfer value at the beginning of the year, as well as the additional value earned in the year.

	Transfer value of accrued pension at 31 December 2009 £000	Change in transfer value over the year £000pa	Transfer value of accrued pension at 31 December 2008 £000pa
Tony Brewer	1,380	230	1,150
Steve Wilson	2,204	129	2,075

This report has been approved by the board and signed on its behalf by

Mike O'Leary
Chairman of the Remuneration committee
19 March 2010

Corporate and Social Responsibility

The company is committed to managing its business in a socially responsible manner. We have a duty to our shareholders to consider social and environmental issues that could affect our business. Our aim is to continually improve our management of the social, environmental and economic issues within our control or influence throughout the business and our supply network. Our corporate and social responsibility ("CSR") programme is designed to address the importance of CSR issues that we face, to encourage and facilitate appropriate management behaviour and be aligned with the group's business strategy taking proper account of the morale and welfare of our employees, the satisfaction of our customers and our impact on the environment. The proper management of CSR also makes good business sense resulting in strategic, commercial and reputational benefits.

The group has reviewed its ongoing CSR policy to ensure that it meets the needs of the markets and communities in which it operates. We communicate our commitment to CSR through the employee handbook and through our group procedures manual. These both include the requirement for employees to undertake to act ethically and responsibly in all of our business dealings with stakeholders and include our ethics, fraud and whistle blowing policies, which are communicated to employees. We do not permit bribery, anti-competition or corrupt practices in any dealings. We are committed to continuous improvements in all aspects of CSR – our policies, our systems, our performance and our reporting.

Our management structure allows the consideration of social and environmental factors by individual businesses within the group and at a group level. Our links with external stakeholders continue to grow including improved customer liaison and community involvement. We aim to manage our relationships with our stakeholders and communicate with them professionally and responsibly. The board has identified its principal stakeholders as shareholders, customers, employees, suppliers and local communities, also recognising its responsibility to the environment.

We monitor our performance against objectives with the aim of continual improvement. In addition to improvements in respect of environmental performance, we have continued to make positive moves in our use of natural resources, waste and energy management, health and safety and staff development and welfare.

Health and safety

The group has a health and safety policy which is endorsed by the board and used throughout the group. The board receives an annual presentation on health and safety matters including detailed facts on health and safety issues and the progress made in improving our performance where required. These reports also outline planned health and safety initiatives and comment on potential future developments and challenges.

The policy seeks to ensure that group operations are carried out at all times in such a manner as to ensure, so far as it is reasonably practicable, compliance with the relevant health and safety legislation in the jurisdictions in which we operate. It also seeks to ensure the health and safety at work of employees and all persons likely to be affected, including contractors, customers, staff and members of the public where appropriate.

All businesses undergo health and safety audits by an external contractor and the measures by which we judge satisfactory outcome are continually reviewed and the standards raised. Each business receives a comprehensive health and safety manual for use as a source of information, guidance and training together with a set of compliance documentation which is reviewed, and updated as necessary, on not less than an annual basis.

Relevant health and safety information and guidance forms part of our induction process and managers are guided and supported in risk assessment techniques. We actively promote health and safety committees at all sites with representation from the various business departments, meeting on a periodic basis and co-ordinated by the health and safety manager on site.

The value of employee participation in delivering this commitment is recognised and management teams are encouraged to create a supportive culture. To achieve this we endeavour to ensure that we:

- continue to improve health and safety systems, procedures and guidance
- make personnel aware of this policy
- maintain high standards of health and safety
- maintain a consistent reporting structure
- provide adequate resources

Training in health and safety includes an awareness of impending changes in relevant legislation and other specialist subjects. The consistent approach taken throughout the group, with the group policy being introduced into recently acquired businesses, improves our governance. In compliance with recently introduced regulations for continuing professional competence, in 2010 and subsequent years, all commercial vehicle drivers are to receive a full days training covering a variety of health and safety and driver related subjects.

Good relationships are maintained with Health and Safety and Environmental Health regulators in the areas in which we operate with positive and prompt responses to any findings and/ or observations following compliance inspections.

As part of the continual development of our policies and procedures, we have during the year reviewed our machinery control procedures and racking inspection processes making some minor modifications. We have also introduced new equipment and procedures in relation to working at height. Whilst we continue to aim for lower levels, the current low frequency of accidents experienced reflects the success of our health and safety policies.

Corporate and Social Responsibility continued

Whilst management is committed to providing a safe working environment with the appropriate working practices and training, this can only be achieved if employees equally give their commitment to a rigorous health and safety culture. Periodic refresher training is undertaken to ensure that this is kept at the forefront. Investment in automated dispatch sortation equipment has significantly reduced manual handling in those businesses where they have been installed.

Audit, inspection and accident report findings are reviewed with action plans produced as necessary to ensure continual improvement in our management of health and safety. All reportable accidents are investigated and, where improvement is required, changes are implemented in a timely manner. There have been no HSE prosecutions in 2009, however the business was subject to the issuance of prohibition and improvement notices as a result of a notifiable accident.

Our people

The importance of good relations and communications with employees is important to the continued success of our business and we seek to provide an environment in which our people can flourish and succeed. Our employees' wellbeing and professional development is central to recruiting and retaining high performing individuals. Our people seek to deliver their best for the business, which combined with a fair and responsive way of doing business, generates a common ambition to add value.

The group remains committed to providing a workplace that is safe and environmentally sound and which complies with applicable laws and regulations. The group expects employees to respect confidential information and company time and assets and believes in open and honest communication, fair treatment and equal opportunities. The group supports the fundamental principles of good governance.

The board values two-way communication between the business unit management and employees on all matters affecting the welfare of the business including regular senior management visits to operating units.

The group's Annual Report and Accounts is available to staff which provides employees with a greater awareness of the group's performance as well as the financial and economic factors that affect it. In addition, those employees who are eligible are also encouraged to become involved in the group's performance through participation in share schemes, including a savings related share scheme.

It is the group's policy that employment opportunities, training, career development and promotion should be available to all, irrespective of age, gender, ethnic origin, religion or disability. Due consideration is given to applications for employment, having regard to the particular aptitudes and abilities of the applicants. Any employee who develops a disability during employment is given the opportunity to retrain for alternative employment where practicable, given the nature of the group's activities.

The group places considerable value on the involvement of its employees and has continued to keep them informed on matters affecting them and on the various factors affecting the performance of the group. It is the group's continued practice to maintain employee participation and involvement in matters which affect their interests through formal and informal meetings.

Recruitment, training and development is designed to ensure the group has suitably skilled and qualified employees to meet the operational needs of the business and offer the opportunity for employees to develop and grow. The group is firmly committed to developing the potential of its people and regularly reviews its succession planning processes. Training is delivered primarily through internal resources with assistance from external providers as and when required. Employee turnover remains low resulting in a stable employee base.

The group considers it important that its employees provide for their retirement and accordingly provides opportunities for them to participate in retirement plans. A group life assurance scheme provides death in service benefits.

Environmental

We continue to reduce each of CO_2 emissions, fuel consumption and vehicle emissions, the amount of waste sent to landfill, the amount of packaging and water consumption. We have continued to improve recycling rates and encourage the use of whole life cost assessments and pollution prevention initiatives.

As a wholesale distributor of floorcoverings and associated products, we operate a number of distribution facilities in the United Kingdom, France, Switzerland and the Netherlands. Whilst we operate specialist tables for the cutting of up to five metre broadloom carpets, we process rather than manufacture. We are therefore not a significant consumer of electricity, gas or water, the consumption of which we seek to reduce through the introduction on repair, renewal or installation of energy or water efficient techniques and equipment. Our electrical requirement is predominantly in respect of fork lift truck battery charging, the operation of the cutting tables and associated mechanical handling and compressed air equipment, office and warehouse lighting and office equipment. Our requirement for gas is predominantly in respect of office heating and limited localised radiant heating within the warehouse. Water consumption is predominantly is respect of employee welfare and commercial vehicle washing. The majority of our water charges are in respect of fixed water rates relating to water discharge from business locations. Actual cost of electricity, gas and water charges in 2009 amounted to 0.25% of sales. Group electricity consumption, where supplied through half hourly meters, will require registration under the carbon reduction commitment scheme due to come into effect later in 2010.

Corporate and Social Responsibility continued

When we invest in new facilities, into which to relocate our businesses, we incorporate modern energy efficient construction techniques and products. It is expected that future projects will incorporate renewable energy solutions and intelligent lighting systems. Due to the nature of our business and with our proactive approach when planning and developing new facilities, we believe that our activities generally have a low impact on the environment, with no environmental legal or compliance issues arising during the year.

The group has a policy to replace the commercial and motor vehicles it operates every five and three years respectively, so improving operational efficiencies and reducing operating costs and vehicle emissions. In line with European Emissions Directives, Euro 4 emission standards for commercial vehicles were introduced in October 2006. This aims to improve the levels of Carbon Monoxide, Hydrocarbon, Nitrogen Oxide and particulate emissions that cause harm to the environment. All of our commercial vehicle fleet complies with Euro 3 emissions standard (introduced in October 2003) and new vehicles delivered from September 2006 conform to the new Euro 4 standards.

Training provided to commercial vehicle drivers during the year, and in respect of obligations imposed by the requirement for continued professional competence in 2010 and subsequent years, includes the necessity of daily vehicle checks and guidance on smooth efficient driving. Our fleet requirements are evaluated on a continual basis so as to ensure the optimum design of transport to maximise capacity and improve aerodynamics.

Our operations predominantly create waste materials in the form of protective plastic wrapping, cardboard and wooden pallets. We continue to sort the plastic and cardboard in discreet types and, with the use of baler units that we have invested in over the last few years, dispatch these to specialist re-processing agents. This has allowed us to reduce the amount of our waste going to landfill and the number of vehicles on the road to collect our waste.

Wooden pallets are recycled where possible or sent to specialist re-processors. In addition we recycle the cardboard poles that are used in the centre of rolls of carpet and vinyl until they are no longer capable of being re-used. In these ways we have further reduced the amount of waste that is sent to landfill sites. Guidance on waste management is issued to the managers of the individual businesses to increase awareness of the need to control waste.

Where appropriate, wrapping and packing materials are sourced from manufacturers where a high proportion of recycled materials are used.

Whilst we have containment and inspection regimes which meet legislative requirements in higher risk areas of the facilities, such as fuel and lubrication stores, compressors and fork lift truck battery charging areas, following a review of these arrangements during the year, we shall be improving fire risk protection in 2010.

We seek to maintain good relationships with national and local regulatory organisations such as the Environment Agency and Environmental Health Departments in the UK. We regularly review regulatory issues and processes are in place to keep up to date. Staff training in health, safety and environmental matters, the frequency and cost associated with which is growing, is important and is reviewed annually as part of normal appraisal processes.

The group continues to use paper recycling and shredding initiatives and has introduced recycling bins for the segregation of aluminium cans, plastics and general waste, having a beneficial impact on the amount recycled.

Achieving sustained growth and profitability

There are a number of key areas whilst seeking to achieve the group's goal of sustained growth and profitability in future years, which will assist in attaining the financial objectives at the same time as meeting our corporate social responsibility obligations.

Through improving our understanding and control of our supply chain, we shall continue to investigate the benefits from using green specification guides and modify our strategy accordingly. We shall continue to work with suppliers to ensure products are supplied from renewable sources, including recycled products, and that their manufacturing processes fairly reward employees and do not seek to exploit.

We place great importance on effectively managing our operations to minimise the likelihood of adverse impact. We proactively manage our facilities to minimise energy consumption utilising energy efficient lighting and heating. Our new sites are subjected to an environmental assessment prior to any construction taking place. This allows solutions to any identified environmental issues to be incorporated into the planning process. Recognising that development can be potentially damaging, we seek to minimise energy consumption during the construction of new premises and the effects on the environment. Wherever possible, subject to the operating constraints of the business, existing trees and vegetation are retained and augmented as necessary. Existing sites are maintained in a tidy condition to minimise ecological impact.

We recognise that our business operations will be around for many years, having an impact on future generations, and to this end we work with local authorities to design new properties which not only comply with guidelines but seek to blend in with their surroundings through the careful use of quality materials, landscaping and design features. We support the desire to see development take place in sustainable locations and we work with transport consultants to formulate green travel plans incorporating car sharing schemes and provision for bicycles when designing new facilities.

Independent Auditor's Report

to the members of Headlam Group plc

We have audited the financial statements of Headlam Group plc for the year ended 31 December 2009 set out on pages 47 to 96. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 28, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's web-site at www.frc.org.uk/apb/scope/UKP.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2009 and of the group's profit for the year then ended;

- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU; and

- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and

- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006; and as regards the group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the director's Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and

- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the director's Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement, set out on page 21, in relation to going concern; and

- the part of the Corporate Governance statement on pages 29 to 35 relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

D Turner

Senior Statutory Auditor

for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
One Snow Hill
Snow Hill Queensway
Birmingham
B4 6GH

19 March 2010

Consolidated Income Statement

for the year ended 31 December 2009

	Note	2009 £000	2008 £000
Revenue	2	**533,793**	557,296
Cost of sales		**(371,533)**	(382,670)
Gross profit		**162,260**	174,626
Distribution expenses		**(100,698)**	(98,517)
Administrative expenses		**(36,804)**	(34,387)
Operating profit	2	**24,758**	41,722
Finance income	6	**3,764**	7,016
Finance expenses	6	**(6,458)**	(8,618)
Net finance costs		**(2,694)**	(1,602)
Profit before tax	3	**22,064**	40,120
Taxation	7	**(6,168)**	(11,433)
Profit for the year attributable to the equity shareholders		**15,896**	28,687
Dividend paid per share	22	**19.70p**	23.10p
Earnings per share			
Basic	9	**19.1p**	34.5p
Diluted	9	**19.1p**	34.5p

All group operations during the financial years were continuing operations.

Consolidated Statement of Comprehensive Income

for the year ended 31 December 2009

	Note	Group 2009 £000	2008 £000
Profit for the year attributable to the equity shareholders		**15,896**	28,687
Other comprehensive income:			
Foreign exchange translation differences arising on translation of overseas operations		**(1,808)**	6,631
Actuarial gains and losses on defined benefit plans	20	**(10,042)**	(4,245)
Effective portion of changes in fair value of cash flow hedges		**(157)**	(800)
Transfers to profit or loss on cash flow hedges		**781**	(48)
Income tax on other comprehensive income		**2,854**	1,304
Other comprehensive (expenses)/income for the year		**(8,372)**	2,842
Total comprehensive income attributable to the equity shareholders for the year		**7,524**	31,529

Statement of Changes in Equity

for the year ended 31 December 2009

Group	Share capital £000	Share premium £000	Capital redemption reserve £000	Translation reserve £000	Cash flow hedging reserve £000	Treasury reserve £000	Retained earnings £000	Total equity £000
Balance at 1 January 2008	4,268	53,512	88	474	–	(11,604)	103,303	150,041
Total comprehensive income for the year	–	–	–	6,631	(848)	–	25,746	31,529
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	–	–	–	–	–	–	426	426
Consideration for purchase of own shares	–	–	–	–	–	(2,204)	–	(2,204)
Share options exercised by employees	–	–	–	–	–	751	–	751
Deferred tax on share options	–	–	–	–	–	–	(227)	(227)
Dividends to equity holders	–	–	–	–	–	–	(19,182)	(19,182)
Total contributions by and distributions to equity shareholders	–	–	–	–	–	(1,453)	(18,983)	(20,436)
Balance at 31 December 2008	4,268	53,512	88	7,105	(848)	(13,057)	110,066	161,134
Balance at 1 January 2009	**4,268**	**53,512**	**88**	**7,105**	**(848)**	**(13,057)**	**110,066**	**161,134**
Total comprehensive income for the year	**–**	**–**	**–**	**(1,808)**	**624**	**–**	**8,708**	**7,524**
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**316**	**316**
Deferred tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**9**	**9**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(16,354)**	**(16,354)**
Total contributions by and distributions to equity shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**(16,029)**	**(16,029)**
Balance at 31 December 2009	**4,268**	**53,512**	**88**	**5,297**	**(224)**	**(13,057)**	**102,745**	**152,629**

Statement of Changes in Equity

for the year ended 31 December 2009

Company	**Share capital £000**	**Share premium £000**	**Capital redemption reserve £000**	**Special reserve £000**	**Cash flow hedging reserve £000**	**Treasury reserve £000**	**Retained earnings £000**	**Total equity £000**
Balance at 1 January 2008	4,268	53,512	88	20,578	–	(11,604)	90,136	156,978
Total comprehensive income for the year	–	–	–	–	(848)	–	10,423	9,575
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	–	–	–	–	–	–	426	426
Consideration for purchase of own shares	–	–	–	–	–	(2,204)	–	(2,204)
Share options exercised by employees	–	–	–	–	–	751	–	751
Dividends to equity holders	–	–	–	–	–	–	(19,182)	(19,182)
Total contributions by and distributions to equity shareholders	–	–	–	–	–	(1,453)	(18,756)	(20,209)
Balance at 31 December 2008	4,268	53,512	88	20,578	(848)	(13,057)	81,803	146,344
Balance at 1 January 2009	**4,268**	**53,512**	**88**	**20,578**	**(848)**	**(13,057)**	**81,803**	**146,344**
Total comprehensive income for the year	**–**	**–**	**–**	**–**	**624**	**–**	**(5,890)**	**(5,266)**
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**316**	**316**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(16,354)**	**(16,354)**
Total contributions by and distributions to equity shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**(16,038)**	**(16,038)**
Balance at 31 December 2009	**4,268**	**53,512**	**88**	**20,578**	**(224)**	**(13,057)**	**59,875**	**125,040**

Balance Sheets

at 31 December 2009

	Note	Group 2009 £000	Group Restated* 2008 £000	Company 2009 £000	Company Restated* 2008 £000
Assets					
Non-current assets					
Property, plant and equipment	10	**96,530**	99,741	**75,082**	75,278
Intangible assets	11	**13,210**	13,210	**–**	–
Investments in subsidiary undertakings	12	**–**	–	**86,392**	86,079
Deferred tax assets	13	**4,731**	1,516	**3,769**	1,441
		114,471	114,467	**165,243**	162,798
Current assets					
Inventories	14	**99,637**	107,597	**–**	–
Trade and other receivables	15	**101,149**	105,942	**27,153**	26,312
Cash and cash equivalents	16	**45,737**	35,193	**27,473**	46,048
Assets held for sale	17	**2,275**	–	**1,387**	–
		248,798	248,732	**56,013**	72,360
Total assets		**363,269**	363,199	**221,256**	235,158
Liabilities					
Current liabilities					
Bank overdraft	16	**(758)**	–	**–**	–
Other interest-bearing loans and borrowings	18	**(900)**	(4,506)	**–**	–
Trade and other payables	19	**(143,216)**	(143,369)	**(41,405)**	(40,153)
Employee benefits	20	**(2,506)**	(2,428)	**(2,506)**	(2,428)
Income tax payable	8	**(8,615)**	(9,546)	**(2,982)**	(5,752)
		(155,995)	(159,849)	**(46,893)**	(48,333)
Non-current liabilities					
Other interest-bearing loans and borrowings	18	**(34,392)**	(30,000)	**(30,000)**	(30,000)
Employee benefits	20	**(20,253)**	(12,216)	**(19,323)**	(10,481)
		(54,645)	(42,216)	**(49,323)**	(40,481)
Total liabilities		**(210,640)**	(202,065)	**(96,216)**	(88,814)
Net assets		**152,629**	161,134	**125,040**	146,344
Equity attributable to equity holders of the parent					
Share capital	22	**4,268**	4,268	**4,268**	4,268
Share premium		**53,512**	53,512	**53,512**	53,512
Other reserves	22	**(7,896)**	(6,712)	**7,385**	6,761
Retained earnings		**102,745**	110,066	**59,875**	81,803
Total equity		**152,629**	161,134	**125,040**	146,344

* See note 1.

These financial statements were approved by the board of directors on 19 March 2010 and were signed on its behalf by:

Tony Brewer
Director

Steve Wilson
Director

Company Number: 460129

Cash Flow Statements

for the year ended 31 December 2009

	Note	Group 2009 £000	Group 2008 £000	Company 2009 £000	Company 2008 £000
Cash flows from operating activities					
Profit before tax for the year		**22,064**	40,120	**218**	4,010
Adjustments for:					
Depreciation, amortisation and impairment		**6,524**	5,305	**1,783**	1,279
Finance income	6	**(3,764)**	(7,016)	**(3,850)**	(8,043)
Finance expense	6	**6,458**	8,618	**5,656**	5,918
Profit on sale of property, plant and equipment		**(102)**	(337)	**(71)**	(304)
Share-based payments	20	**316**	426	**3**	128
Operating profit before changes in working capital and other payables		**31,496**	47,116	**3,739**	2,988
Change in inventories		**6,618**	(1,480)	**–**	–
Change in trade and other receivables		**3,028**	876	**(148)**	379
Change in trade and other payables		**2,511**	(19,096)	**530**	(5,068)
Cash generated/(utilised) from the operations		**43,653**	27,416	**4,121**	(1,701)
Interest paid		**(2,272)**	(4,552)	**(1,458)**	(1,200)
Tax (paid)/received		**(7,425)**	(11,012)	**(1,568)**	606
Additional contributions to defined benefit plan		**(2,607)**	(1,147)	**(2,407)**	(887)
Net cash flow from operating activities		**31,349**	10,705	**(1,312)**	(3,182)
Cash flows from investing activities					
Proceeds from sale of property, plant and equipment		**664**	1,309	**508**	959
Interest received		**846**	2,997	**613**	2,801
Dividends received		**–**	–	**1,375**	9,586
Acquisition of subsidiaries, net of cash acquired	24	**–**	(726)	**–**	–
Acquisition of property, plant and equipment	10	**(7,313)**	(10,664)	**(3,405)**	(3,616)
Net cash flow from investing activities		**(5,803)**	(7,084)	**(909)**	9,730
Cash flows from financing activities					
Proceeds from the issue of treasury shares		**–**	751	**–**	751
Proceeds from borrowings		**1,152**	33,726	**–**	30,000
Payment to acquire own shares		**–**	(2,204)	**–**	(2,204)
Dividends paid	22	**(16,354)**	(19,182)	**(16,354)**	(19,182)
Net cash flow from financing activities		**(15,202)**	13,091	**(16,354)**	9,365
Net increase/(decrease) in cash and cash equivalents		**10,344**	16,712	**(18,575)**	15,913
Cash and cash equivalents at 1 January		**35,193**	16,702	**46,048**	30,135
Effect of exchange rate fluctuations on cash held		**(558)**	1,779	**–**	–
Cash and cash equivalents at 31 December	16	**44,979**	35,193	**27,473**	46,048

The company's profit before tax excludes dividends received from subsidiaries.

Notes to the Financial Statements

1 ACCOUNTING POLICIES

Headlam Group plc (the "company") is a company incorporated in the UK.

The group Financial Statements consolidate those of the company and its subsidiaries which together are referred to as the "group". The company's Financial Statements present information about the company as a separate entity and not about its group.

Both the company's Financial Statements and the group's Financial Statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards as adopted by the EU ("adopted IFRS"). On publishing the company's Financial Statements here together with the group Financial Statements, the company is taking advantage of the exemption in s408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved Financial Statements.

The principal accounting policies applied in the preparation of the Financial Statements of the company and the Financial Statements of the group are set out below. These policies have been applied consistently to all years presented, unless otherwise stated.

Judgements made by the directors, in the application of these accounting policies that have significant effect on the Financial Statements and estimates with a significant risk of material adjustment in the next year are discussed below.

Restatement

Deferred tax balances in the 2008 Consolidated Balance Sheet have been reclassified to disclose deferred tax balances as a net amount, being an asset of £1,516,000 as required by IAS 12. Previously these amounts were shown as separate deferred tax assets of £5,372,000 and deferred tax liabilities of £3,856,000.

Impact of newly adopted accounting standards

During the year the group has adopted the following new standards and interpretations:

The adoption of IFRS 8 'Operating Segments' requires operating segments to be identified on the basis of internal reports used to assess performance and allocate resources by the Group Chief Executive, the group's chief operating decision maker. The adoption of this standard has not resulted in any change to the segments previously reported.

The adoption of IAS 1 (Revised) 'Presentation of Financial Statements' means that all owner and non-owner changes in equity are now presented within the Consolidated Statement of Changes in Equity and all non-owner changes in equity are presented within the Consolidated Statement of Comprehensive Income. Since the changes are presentational only, there is no impact on profit, earnings per share or net assets. Comparative information has been re-presented accordingly.

Revised IAS 23 'Borrowing Costs' requires the group to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of the asset. Previously, group subsidiaries immediately recognised all borrowing costs as an expense. Revised IAS 23 has been applied prospectively from 1 January 2009. The impact on the Consolidated Financial Statements for the year ended 31 December 2009 has been that £113,000 of directly attributable borrowing costs have been capitalised in respect of the group's property development in the Netherlands, see note 18.

IFRIC 14 ' The limit on a defined benefit asset, minimum funding requirements and their interaction' limits the amount of defined benefit pension assets which can be recognised on certain schemes where the group does not have an unconditional right to a refund of any surplus which may exist. This results in a de-recognition of any surplus and the recognition of a liability for deficit funding arrangements. The adoption of IFRIC 14 has had no impact on the profit, earnings per share or net assets for the year ended 31 December 2009 or from its retrospective application.

The amendment to IFRS 2 'Share-based Payment - Vesting Conditions and Cancellations' clarifies the definition of vesting conditions, introduces the concept of non-vesting conditions, requires non-vesting conditions to be reflected in grant date fair value and provides the accounting treatment for non-vesting conditions and cancellations. The amendment has had no effect on the group's Consolidated Financial Statements.

The amendments to IFRS 7 'Improving disclosures about financial instruments' requires enhanced disclosures about fair value measurements of financial instruments, including using a three-level fair value hierarchy that prioritises the inputs to valuation techniques used in fair value calculations. The amended standard also requires improved disclosures relating to liquidity risk. The adoption of this amendment has had no impact on the profit, earnings per share or net assets for the year ended 31 December 2009.

IFRS not yet applied

The following relevant standards and interpretations have been published, endorsed by the EU, and are available for early adoption but have not yet been applied by the group in the Consolidated Financial Statements for the year ended 31 December 2009.

Revised IFRS 3 'Business Combinations (2008)' incorporates certain changes that amend the group's current accounting policies in respect of business combinations, the main change being that transaction costs, other than share and debt issue costs, will be expensed as incurred. Revised IFRS 3 becomes mandatory for the group's 2010 Consolidated Financial Statements and will be applied prospectively.

Amended IAS 27 'Consolidated and Separate Financial Statements (2008)' requires accounting for changes in ownership interests by the group in a subsidiary, while maintaining control, to be recognised as an equity transaction. When the group loses control of a subsidiary, any interest retained in the former subsidiary will be measured at fair value with the gain or loss recognised in profit or loss. The amendments to IAS 27, which becomes mandatory for the group's 2010 Consolidated Financial Statements, are not expected to have a significant impact on the group's Consolidated Financial Statements.

IFRIC 16 'Hedges of a Net Investment in a Foreign Operation', IFRIC 17 'Distributions of Non Cash Assets to Owners' and IFRIC 18 'Transfers of Assets from Customers'. There will be no impact upon the group's Consolidated Financial Statements from these interpretations.

The following have been published but not yet been endorsed by the EU:

Amendment to IFRS 2 'Group Cash Settled Share-based Payment Transactions', IFRS 9 'Financial Instruments', Amendment to IFRIC 14 'Prepayments of Minimum Funding Requirement', IFRIC 19 'Extinguishing Financial Liabilities with Equity Instruments' and IAS 24 'Related Party Disclosures'. Management is currently assessing the impact of these standards and interpretations on the group's Consolidated Financial Statements.

The annual improvements to International Financial Reporting Standards (IFRSs) project provides a vehicle for making non-urgent but necessary amendments to IFRSs. The 2009 annual improvements project makes amendments to a number of standards. These amendments were issued but not effective for the year ended 31 December 2009 and are not expected to have a material impact on the group's Consolidated Financial Statements.

Measurement convention

The company and group Financial Statements are prepared on the historical cost basis with the exception of derivative financial instruments which are stated at fair value. Non-current assets held for sale are stated at the lower of previous carrying amount and fair value less costs to sell.

Basis of consolidation

Subsidiaries are entities controlled by the group. Control exists when the group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account.

The financial statements of subsidiaries are included in the group's Consolidated Financial Statements from the date that control commences until the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the group.

Inter-company transactions, balances and unrealised gains and losses on transactions between group companies are eliminated in the group's Consolidated Financial Statements.

Accounting estimates and judgements

The board are responsible for the development, selection and disclosure of the group's critical accounting policies and estimates and the application of these policies and estimates. In applying the accounting policies, appropriate estimates have been made in a number of areas and the actual outcome may differ from the position described in the company's and group's Balance Sheet at 31 December 2009. The key sources of estimation uncertainty at the balance sheet date that may give rise to a material adjustment to the carrying value of assets and liabilities within the next financial year are as follows:

Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairment losses.

The group is committed to investing in new facilities where existing facilities fail to provide satisfactory customer service in a cost effective manner. When construction on a new facility commences, the existing facility is marketed for sale and this action can on occasions give rise to an adverse difference between cost and fair value. It has been assumed that at the balance sheet date, fair value exceeds cost. This is formally assessed for all properties on a triennial basis. At the latest review, carried out at 31 December 2007, the fair value of UK freehold and long leasehold land and buildings exceeded cost by £12,100,000.

Goodwill impairment

The outcome of the group's annual impairment test for goodwill is dependent on the forecast cash flows of each cash-generating unit together with key management assumptions including profit growth and discount rates. No impairment resulted from the annual impairment test for 2009.

Deferred tax assets

Deferred tax assets are recognised at the balance sheet date based on the assumption that there is a high expectation that the asset will be realised in due course. This assumption is dependent on the group's ability to generate sufficient future taxable profits.

Employee benefits

The deficit relating to the group's defined benefit plans is assessed annually in accordance with IAS 19 and after taking independent actuarial advice. The principle assumptions are set out in note 19. The amount of the deficit is dependent on plan asset and liability values and the actuarial assumptions used to determine the deficit.

The assumptions include asset growth rates, pension and salary increases, price inflation, discount rate used to measure actuarial liabilities and mortality rates.

Notes to the Financial Statements
continued

Foreign currency
Foreign currency transactions
Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

Financial statements of overseas operations
The assets and liabilities of overseas subsidiaries, including goodwill and fair value adjustments arising on consolidation, are translated at foreign exchange rates ruling at the balance sheet date.

The revenues and expenses of foreign subsidiaries are translated at an average rate for the period where this rate approximates to the foreign exchange rates ruling at the dates of the transactions.

Exchange differences arising from this translation of foreign subsidiaries are taken directly to the translation reserve and reflected as a movement in the Statement of Comprehensive Income.

Foreign currency exposure
Note 23 contains information about the foreign currency exposure of the group and risks in relation to foreign exchange movements.

Classification of financial instruments issued by the group
Financial instruments issued by the group are treated as equity, i.e. forming part of shareholders' funds, only to the extent that they meet the following two conditions:

(a) they include no contractual obligations upon the company, or group as the case may be, to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the company or group; and

(b) where the instrument will or may be settled in the company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the company's own equity instruments or is a derivative that will be settled by the company exchanging a fixed amount of cash or other financial assets for a fixed number or its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the company's own shares, the amounts presented in these Financial Statements for called up share capital and share premium account exclude amounts in relation to those shares.

Finance payments associated with financial liabilities are dealt with as part of financial expenses. Finance payments associated with financial instruments that are classified in equity are dividends and are recorded directly in equity.

Derivative financial instruments
The group holds derivative financial instruments to hedge its foreign currency and interest rate risk exposures. Derivatives are recognised initially at fair value; attributable transaction costs are recognised in the income statement when incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are accounted for as described below.

Cash flow hedges
Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognised directly in equity to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in the income statement. If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in equity is transferred to the carrying amount of the asset when it is recognised. In other cases the amount recognised in equity is transferred to the income statement in the same period that the hedged item affects profit or loss.

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

The fair value of forward exchange contracts is their quoted market price at the balance sheet date, being the present value of the quoted forward price. The gain or loss on remeasurement to fair value of forward exchange contracts is recognised immediately in the income statement.

Property, plant and equipment
Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and any other costs directly attributable to bringing the asset to a working condition for its intended use.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

Depreciation is charged to the income statement on a straight-line basis over their estimated useful lives. Land is not depreciated. The annual rates applicable are:

Freehold and long leasehold properties	– 2%
Short leasehold properties	– period of lease
Motor vehicles	– 25%
Office and computer equipment	– 10%-33.3%
Warehouse and production equipment	– 10%-20%

Notes to the Financial Statements
continued

Goodwill and other intangible assets
Goodwill
All business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of subsidiaries. In respect of business acquisitions that have occurred since 1 January 2004, goodwill represents the difference between the cost of the acquisition and the fair value of the identifiable assets, liabilities and contingent liabilities acquired.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is not amortised but, tested annually for impairment.

In respect of acquisitions prior to 1 January 2004, goodwill is included on the basis of its deemed cost, which represents the amount recorded under UK GAAP which was broadly comparable save that only separable intangibles were recognised and goodwill was amortised. This is in accordance with IFRS 1.

Other intangibles
Other intangible assets that are acquired by the group are stated at cost less accumulated amortisation and impairment losses. Intangible assets recognised as a result of a business combination are stated at fair value at the date of acquisition less cumulative amortisation and impairment losses.

Amortisation
Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. Intangible assets with an indefinite useful life and goodwill are systematically tested for impairment at each balance sheet date. Other intangible assets are amortised from the date they are available for use. The estimated useful lives of customer lists are deemed to be between 1 – 24 months.

Non-current assets held for sale
A non-current asset is classified as held for sale if its carrying amount will be recovered principally through sale rather than through continuing use, it is available for immediate sale and sale is highly probable within one year.

On initial classification as held for sale, non-current assets and disposal groups are measured at the lower of previous carrying amount and fair value less costs to sell with any adjustments taken to the Income Statement. The same applies to gains and losses on subsequent remeasurement.

Trade and other receivables
Trade and other receivables are initially stated at fair value and subsequently at amortised cost less impairment losses. Debts are provided for, the credit loss allowance, on specific receivables in full as soon as they are known to be 'bad' or it becomes apparent that payment is 'doubtful'.

Inventories
Inventories are stated at the lower of cost and net realisable value. Cost is based on the first-in first-out principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Inventory provisions are determined by reference to each individual product and are calculated by assessing the age, condition and quantity of each individual product.

Cash and cash equivalents
Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of cash management of both the company and group are included as a component of cash and cash equivalents for the purpose only of the Cash Flow Statement.

Trade payables
Trade payables are initially recognised at fair value and then are stated at amortised cost.

Impairment
The carrying amounts of the group's assets other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets recoverable amount is estimated.

For goodwill and intangible assets that are not yet available for use, the recoverable amount is estimated at each balance sheet date.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then to reduce the carrying amount of the other assets in the unit on a pro-rata basis. A cash generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

Calculation of recoverable amount
The recoverable amount of the group's receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate, i.e., the effective interest rate computed at initial recognition of these financial assets. Receivables with a short duration are not discounted.

Notes to the Financial Statements
continued

The recoverable amount of other assets is the greater of their fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Reversals of impairment
An impairment loss in respect of goodwill is not reversed.

In respect of other assets, an impairment loss is reversed when there is an indication that the impairment loss may no longer exist and there had been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the assets carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Interest-bearing borrowings
Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

Borrowing costs
Borrowing costs are capitalised where the group constructs qualifying assets. All other borrowing costs are written off to the income statement as incurred.

Borrowing costs are charged to the income statement using the effective interest rate method.

Employee benefits
The company and the group operate both defined benefit and defined contribution plans, the assets of which are held in independent trustee administered funds. The pension cost is assessed in accordance with the advice of a qualified actuary.

Defined contribution plans
Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

Defined benefit plans
The group's net obligation in respect of defined benefit pension plans is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is discounted to determine its present value, and the fair value of any plan assets, at bid price, is deducted.

The liability discount rate is the yield at the balance sheet date using AA rated corporate bonds that have maturity dates approximating to the terms of the group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the income statement on a straight-line basis over the average period until the benefits become vested.

To the extent that the benefits vest immediately, the expense is recognised immediately in the income statement.

All actuarial gains and losses that arise in calculating the group's obligation in respect of a scheme are recognised immediately in reserves and reported in the Statement of Comprehensive Income.

Where the calculation results in a benefit to the group, the asset recognised is limited to the present value of any future refunds from the plan or reductions in future contributions to the plan.

The group operates a UK defined benefit pension plan and a defined benefit plan in Switzerland. In the UK as there is no contractual agreement or stated group policy for allocating the net defined benefit liability between the participating subsidiaries and as such the full deficit is recognised by the company, which is the sponsoring employer. The participating subsidiary companies have recognised a cost equal to contributions payable for the period as advised by a professionally qualified actuary.

Share-based payment transactions
The company and group operate various equity settled share option schemes under the approved and unapproved executive schemes and savings related schemes.

For executive share option schemes, the option price may not be less than the mid market value of the group's shares at the time when the options were granted or the nominal value.

Approved
These share option awards are subject to the movement of the group's earnings per share exceeding RPI over the relevant period.

Unapproved
These share option awards are subject to the movement of the group earnings per share exceeding RPI between 3% and 5% per annum.

The performance is assessed by reference to the group's published results.

The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The fair value of the options granted is measured using an option valuation model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where forfeiture is due only to share prices not achieving the threshold for vesting.

When options are granted to employees of subsidiaries of the company, the fair value of options granted is recognised as an employee expense in the financial statements of the subsidiary undertaking together with the capital contribution received. In the financial statements of the company, the options granted are recognised as an investment in subsidiary undertakings with a corresponding increase in equity.

Repurchase of share capital
When share capital recognised as equity is repurchased, the amount of the consideration paid, net of any tax effects is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold or reissued subsequently, the amount received is recognised as an increase in equity, and the resulting surplus or deficit on the transaction is transferred to or from retained earnings.

Revenue
Revenue from the sale of goods is measured at the fair value of the consideration, net of trade discounts and excludes intra-group sales and value added and similar taxes. Revenue from the sale of goods is recognised when the significant risks and rewards of ownership of the goods are transferred to the buyer (which is ordinarily the date at which goods are despatched from a distribution facility), the amount of revenue can be reliably measured and it is probable that the economic benefits associated with the transaction will flow to the group.

Operating lease payments
Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

Net financing costs
Net financing costs comprise interest payable, finance charges on shares classified as liabilities, finance leases, interest receivable on funds invested, foreign exchange gains and losses and gains and losses on hedging instruments as outlined in the accounting policy relating to derivative financial instruments and hedging described above.

Interest income and interest payable is recognised in the income statement as it accrues, using the effective interest method. Dividend income is recognised in the income statement on the date the entity's right to receive payments is established.

The expected return on assets of funded defined benefits pension plans, less administration expenses of pension plans are recognised in financial income. The interest accruing on defined benefit pension plan liabilities are recognised in financial expenses.

Taxation
Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Notes to the Financial Statements
continued

2 SEGMENT REPORTING

The group has 54 operating segments which represent the individual trading operations throughout the UK (49 segments) and Continental Europe (5 segments). Each of the operations is principally aligned to the sales, marketing, supply and distribution of floorcovering products. The operating results of each are regularly reviewed by the Chief Operating Decision Maker, which is deemed to be the Group Chief Executive. Discrete financial information is available for each segment and used by the Group Chief Executive for decisions on resource allocation and to assess performance.

The operating segments have been aggregated to the extent that they have similar economic characteristics, with relevance to products/services, type and class of customer, methods of sale and distribution and the regulatory environment in which they operate. The group's internal management structure and financial reporting systems differentiate the operating segments on the basis of the differing regulatory and economic environment in the UK and Continental Europe and accordingly report these as two separate reportable segments. This distinction is embedded in the construction of operating reports reviewed by the Group Chief Executive, the board and the executive management team and forms the basis for the presentation of operating segment information given below.

	UK		Continental Europe		Total	
	2009 £000	2008 £000	**2009 £000**	2008 £000	**2009 £000**	2008 £000
Revenue						
External revenues	**429,646**	458,572	**104,147**	98,724	**533,793**	557,296
Depreciation	**2,834**	2,929	**733**	537	**3,567**	3,466
Amortisation	**–**	44	**–**	257	**–**	301
Reportable segment result	**23,106**	39,174	**2,487**	3,574	**25,593**	42,748
Reportable segment assets	**223,044**	220,832	**49,636**	54,701	**272,680**	275,533
Capital expenditure	**926**	2,295	**2,197**	384	**3,123**	2,679
Reportable segment liabilities	**(123,088)**	(117,052)	**(20,662)**	(25,470)	**(143,750)**	(142,522)

During the year there have been no inter segment revenues (2008: £nil).

Reconciliations of reportable segment profit, assets and liabilities and other material items:

	2009 £000	2008 £000
Profit for the year		
Total profit for reportable segments	**25,593**	42,748
Impairment of assets	**(1,211)**	–
Unallocated income/(expense)	**376**	(1,026)
Operating profit	**24,758**	41,722
Finance income	**3,764**	7,016
Finance expense	**(6,458)**	(8,618)
Profit before taxation	**22,064**	40,120
Taxation	**(6,168)**	(11,433)
Profit for the year	**15,896**	28,687

Notes to the Financial Statements
continued

2 SEGMENT REPORTING continued

	2009 £000	2008 £000
Assets		
Total assets for reportable segments	**272,680**	275,533
Unallocated assets:		
Properties, plant and equipment	**83,583**	86,150
Deferred tax assets	**4,731**	1,516
Assets held for sale	**2,275**	–
Total assets	**363,269**	363,199
Liabilities		
Total liabilities for reportable segments	**(143,750)**	(142,522)
Unallocated liabilities:		
Employee benefits	**(22,759)**	(14,643)
Net borrowings	**(35,292)**	(34,506)
Income tax payable	**(8,615)**	(9,546)
Derivative liabilities	**(224)**	(848)
Total liabilities	**(210,640)**	(202,065)

	Reportable segment totals £000	Group items £000	Consolidated totals £000
Other material items 2009			
Capital expenditure	**3,123**	**4,190**	**7,313**
Depreciation	**3,567**	**1,746**	**5,313**
Impairment of assets	**–**	**1,211**	**1,211**
	6,690	**7,147**	**13,837**
Other material items 2008			
Capital expenditure	2,679	7,985	10,664
Depreciation	3,466	1,538	5,004
	6,145	9,523	15,668

Each segment is a continuing operation.

Notes to the Financial Statements
continued

2 SEGMENT REPORTING continued

The Group Chief Executive, the board and the executive management team has access to information that provides details on revenue by principal product group for the two reportable segments, as set out in the following table.

Revenue by principal product group is summarised below:

	UK		Continental Europe		Total	
	2009 £000	2008 £000	2009 £000	2008 £000	2009 £000	2008 £000
Revenue						
Carpet	185,805	197,572	13,897	14,110	199,702	211,682
Rugs	11,496	10,758	–	–	11,496	10,758
Commercial	133,686	142,613	44,190	41,926	177,876	184,539
Underlay	14,849	16,384	381	344	15,230	16,728
Domestic vinyl	47,743	56,147	13,509	11,456	61,252	67,603
Wood & laminate	29,829	28,500	23,909	22,189	53,738	50,689
Miscellaneous	6,238	6,598	8,261	8,699	14,499	15,297
	429,646	458,572	104,147	98,724	533,793	557,296

3 PROFIT BEFORE TAX

The following are included in profit before tax:

	2009 £000	2008 £000
Depreciation on property, plant and equipment	5,313	5,004
Amortisation of intangible assets	–	301
Impairment of assets	1,211	–
Profit on sale of property, plant and equipment	102	337
Operating lease rentals		
Plant and machinery	9,001	8,992
Land and buildings	1,951	2,209

Auditor's remuneration:

	2009 £000	2008 £000
Audit of these financial statements	60	60
Amounts received by the auditors and their associates in respect of:		
Audit of financial statements of subsidiaries pursuant to legislation	156	145
All other services	2	16
	218	221

Amounts paid to the company's auditor in respect of services to the company, other than the audit of the company's Financial Statements, have not been disclosed as the information is required instead to be disclosed on a consolidated basis.

Notes to the Financial Statements
continued

4 STAFF NUMBERS AND COSTS

The average number of people employed, including directors, during the year, analysed by category, was as follows:

	Number of employees Group	
	2009	2008
By sector:		
Floorcoverings	**2,023**	2,178
Central operations	**9**	9
	2,032	2,187
By function:		
Sales and distribution	**1,865**	2,011
Administration	**167**	176
	2,032	2,187

The aggregate payroll costs were as follows:

	£000	£000
Wages and salaries	**63,012**	59,879
Equity settled transactions	**316**	426
Social security costs	**8,375**	7,705
Pension costs	**2,817**	3,195
	74,520	71,205

5 DIRECTORS' EMOLUMENTS

	2009 £000	2008 £000
Directors emoluments	**1,898**	1,515
Gains made on share options	**–**	33
Share based payment	**2**	116

Further details of directors' emoluments, share options and pension entitlement are given in the Remuneration Report on pages 36 to 42.

Notes to the Financial Statements

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6 FINANCE INCOME AND EXPENSE

	2009 £000	2008 £000
Interest income:		
Bank interest	**641**	2,902
Other	**62**	209
Return on defined benefit plan assets	**3,061**	3,905
Finance income	**3,764**	7,016
Interest expense:		
Bank loans, overdrafts and other financial expenses	**(2,256)**	(4,543)
Interest on defined benefit plan obligation	**(4,202)**	(4,075)
Finance expenses	**(6,458)**	(8,618)

7 TAXATION

Recognised in the income statement

	2009 £000	2008 £000
Current tax expense:		
Current year	**7,121**	11,388
Adjustments for prior years	**(601)**	(1,411)
	6,520	9,977
Deferred tax expense:		
Origination and reversal of temporary differences	**(360)**	(229)
Effect of change in UK tax law	**–**	7
Adjustments for prior years	**8**	1,678
	(352)	1,456
Total tax in income statement	**6,168**	11,433

Tax relating to items credited/(charged) to equity

	2009 £000	2008 £000
Current tax on:		
Income and expenses recognised directly in equity	**–**	211
Deferred tax on:		
Share options	**9**	(227)
Deferred tax on other comprehensive income:		
Defined benefit plans	**2,791**	1,093
Cash flow hedge	**63**	–
Total tax reported directly in reserves	**2,863**	1,077

Current tax on income and expenses recognised directly in equity of £nil (2008: £211) represents the current tax on share based payments.

Notes to the Financial Statements
continued

7 TAXATION continued

Reconciliation of effective tax rate

	2009		2008	
	%	£000	%	£000
Profit before tax		**22,064**		40,120
Tax using the UK corporation tax rate	**28%**	**6,178**	28.5%	11,433
Effect of change in UK tax law	**–**	**–**	–	7
Non-deductible expenses	**3.0%**	**658**	0.3%	126
Effect of tax rates in foreign jurisdictions	**(0.3%)**	**(75)**	(1.0%)	(400)
(Over)/under provided in prior years	**(2.7%)**	**(593)**	0.7%	267
Total tax in income statement	**28%**	**6,168**	28.5%	11,433

8 CURRENT TAX LIABILITIES

The group's current tax liability of £8,615,000 (2008: £9,546,000) represents the amount of income tax payable in respect of current and prior year periods which exceed any amounts recoverable. The company's current tax liability of £2,982,000 (2008: £5,752,000) represents the amount of income tax payable in respect of current and prior year periods which exceed any amounts recoverable.

9 EARNINGS PER SHARE

	2009 £000	2008 £000
Earnings		
Earnings for the purposes of basic earnings per share being profit attributable to equity holders of the parent	**15,896**	28,687

	2009	2008
Number of shares		
Issued ordinary shares at 1 January	**85,363,743**	85,363,743
Effect of shares held in treasury	**(2,248,647)**	(2,223,206)
Weighted average number of ordinary shares for the purposes of basic earnings per share	**83,115,096**	83,140,537
Effect of diluted potential ordinary shares:		
Weighted average number of ordinary shares at 31 December	**83,115,096**	83,140,537
Share options	**595,162**	433,308
Number of shares that would have been issued at fair value	**(500,540)**	(401,137)
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**83,209,718**	83,172,708

At 31 December 2009, the company held 2,248,647 shares in treasury and these are excluded from the calculation of earnings per share.

Notes to the Financial Statements
continued

10 PROPERTY, PLANT AND EQUIPMENT

Group	Land & buildings £000	Plant & equipment £000	Under construction £000	Total £000
Cost				
Balance at 1 January 2008	83,920	23,839	2,250	110,009
Additions	181	2,686	7,797	10,664
Disposals	(637)	(2,353)	(6)	(2,996)
Effect of movements in foreign exchange	2,765	1,791	906	5,462
Transfer to use	5,546	165	(5,711)	–
Balance at 31 December 2008	91,775	26,128	5,236	123,139
Balance at 1 January 2009	91,775	26,128	5,236	123,139
Additions	4,126	3,187	–	7,313
Disposals	(536)	(1,816)	–	(2,352)
Effect of movements in foreign exchange	(778)	(563)	(420)	(1,761)
Transfer to use	4,816	–	(4,816)	–
Transfer to assets held for sale	(3,961)	–	–	(3,961)
Balance at 31 December 2009	95,442	26,936	–	122,378
Depreciation				
Balance at 1 January 2008	8,132	9,780	–	17,912
Depreciation charge for the year	1,570	3,434	–	5,004
Disposals	(63)	(1,960)	–	(2,023)
Effect of movements in foreign exchange	1,150	1,355	–	2,505
Balance at 31 December 2008	10,789	12,609	–	23,398
Balance at 1 January 2009	10,789	12,609	–	23,398
Depreciation charge for the year	1,736	3,577	–	5,313
Disposals	(104)	(1,686)	–	(1,790)
Effect of movements in foreign exchange	(321)	(437)	–	(758)
Transfer to assets held for sale	(315)	–	–	(315)
Balance at 31 December 2009	11,785	14,063	–	25,848
Net book value				
At 1 January 2008	75,788	14,059	2,250	92,097
At 31 December 2008 and 1 January 2009	80,986	13,519	5,236	99,741
At 31 December 2009	**83,657**	**12,873**	**–**	**96,530**

Notes to the Financial Statements
continued

10 PROPERTY, PLANT AND EQUIPMENT continued

Company	Land & buildings £000	Plant & equipment £000	Under construction £000	Total £000
Cost				
Balance at 1 January 2008	76,985	559	2,245	79,789
Additions	112	38	3,466	3,616
Disposals	(516)	(3)	–	(519)
Transfer to group company	–	–	(165)	(165)
Transfer to use	5,546	–	(5,546)	–
Balance at 31 December 2008	82,127	594	–	82,721
Balance at 1 January 2009	82,127	594	–	82,721
Additions	3,290	115	–	3,405
Disposals	(516)	(64)	–	(580)
Transfer to group company	–	(44)	–	(44)
Transfer to assets held for sale	(1,890)	–	–	(1,890)
Balance at 31 December 2009	83,011	601	–	83,612
Depreciation				
Balance at 1 January 2008	5,692	501	–	6,193
Depreciation charge for the year	1,249	30	–	1,279
Disposals	(26)	(3)	–	(29)
Balance at 31 December 2008	6,915	528	–	7,443
Balance at 1 January 2009	6,915	528	–	7,443
Depreciation charge for the year	1,392	38	–	1,430
Disposals	(88)	(61)	–	(149)
Transfer to group company	–	(36)	–	(36)
Transfer to assets held for sale	(158)	–	–	(158)
Balance at 31 December 2009	8,061	469	–	8,530
Net book value				
At 1 January 2008	71,293	58	2,245	73,596
At 31 December 2008 and 1 January 2009	75,212	66	–	75,278
At 31 December 2009	**74,950**	**132**	**–**	**75,082**

Notes to the Financial Statements
continued

11 INTANGIBLE ASSETS – GROUP

	Goodwill £000	Customer lists £000	Total £000
Cost			
Balance at 1 January 2008	13,210	3,879	17,089
Addition (note 24)	–	263	263
Balance at 31 December 2008	13,210	4,142	17,352
Balance at 1 January 2009 and 31 December 2009	13,210	4,142	17,352
Amortisation			
Balance at 1 January 2008	–	3,879	3,879
Amortisation for the year	–	301	301
Effect of movements in foreign exchange	–	(38)	(38)
Balance at 31 December 2008	–	4,142	4,142
Balance at 1 January 2009 and 31 December 2009	–	4,142	4,142
Net book value			
At 1 January 2008 and 31 December 2008	13,210	–	13,210
At 1 January 2009 and 31 December 2009	**13,210**	**–**	**13,210**

Cumulative impairment recognised in relation to goodwill is £nil.

Amortisation
The amortisation charge is recognised in administration expenses in the Consolidated Income Statement.

Impairment tests for cash-generating units containing goodwill
Goodwill is attributed to the businesses identified below for the purpose of testing impairment. These businesses are the lowest level at which goodwill is monitored and are a sub-classification of the group's operating segments.

The aggregate carrying amounts of goodwill allocated to each unit are as follows:

	Reported Segment	2009 £000	2008 £000
Joseph, Hamilton & Seaton	UK	**4,348**	4,348
Crucial Trading	UK	**1,369**	1,369
Belcolor AG	Continental Europe	**3,342**	3,342
LMS SA	Continental Europe	**3,197**	3,197
Other	UK	**954**	954
		13,210	13,210

11 INTANGIBLE ASSETS – GROUP continued

Impairment
Each year, whenever events or a change in the economic environment indicates a risk of impairment, the group reviews the value of goodwill balances allocated to its cash generating units. In the absence of any identified impairment risks, tests are performed based on internal valuations of each cash generating unit.

An impairment test is a comparison of the carrying value of the assets of a business or cash generating unit ("CGU") to their recoverable amount. Where the recoverable amount is less than the carrying value, an impairment results. During the year, all goodwill was tested for impairment, with no impairment charge resulting and the value of goodwill being recovered for each CGU within a six year period.

Value in use was determined by discounting the future cash flows generated from the continuing use of the CGU on a basis consistent with 2008.

Cash flows were projected based on past experience, actual operating results and the approved forecasts for 2010. For the purpose of impairment testing the forecast cash flows for the period 2011 – 2014 assumed a 1% growth rate. Cash flows for a further 20 year period were extrapolated using a constant growth rate of 1% which does not exceed the long-term average growth rate obtained from relevant industrial comparisons.

Key assumptions
The main assumptions within the operating cash flows used for 2010 include the achievement of future sales volumes and prices for all key product lines, control of purchase prices, achievement of budgeted operating costs and no significant adverse foreign exchange rate movements. These assumptions have been reviewed in light of the current economic environment which has resulted in more conservative estimates about the future.

Management has estimated the discount rate by reference to past experience and an industry average weighted average cost of capital. This has been adjusted to include an appropriate risk factor to reflect current economic circumstances and the risk profile of the CGU's. A post tax weighted average cost of capital of 9.5% (2008: 10.1%) has been used for impairment testing, pre-tax 12.3% (2008: 15%), adjusted to 10.5% (2008: 11.1%) for Continental Europe to reflect the differing risk profile of that operating segment.

The CGU's in the UK have similar characteristics, and risk profiles, and therefore a single discount rate has been applied to each UK CGU. Similarly, the directors view the CGU's in Continental Europe as having consistent risk profiles and therefore a single risk factor has been applied. The CGU's in Continental Europe operate under a different regulatory environment and this is therefore reflected in the risk factor used to determine the discount rates in the UK and Continental Europe.

Sensitivity analysis
The group's estimate of impairments are most sensitive to increases in the discount rate and forecast cash flows. Sensitivity analysis has been carried out by reference to both of these assumptions and neither a 1% increase in the discount rate or a 5% reduction in forecast cash flows would result in any impairment..

Other than disclosed above, any reasonable change to the key assumptions would be unlikely to generate a different impairment test outcome to the one that is included in these Financial Statements.

Notes to the Financial Statements
continued

12 INVESTMENTS IN SUBSIDIARIES

Summary information on investments in subsidiary undertakings is as follows:

	£000
Cost	
Balance at 1 January 2008	87,941
Share options granted to employees of subsidiary undertakings	298
Balance at 31 December 2008	88,239
Balance at 1 January 2009	88,239
Share options granted to employees of subsidiary undertakings	313
Balance at 31 December 2009	88,552
Provisions	
Balance at 1 January 2008 and 31 December 2008	2,160
Balance at 1 January 2009 and 31 December 2009	2,160
Carrying value	
At 1 January 2008	85,781
At 31 December 2008	86,079
At 31 December 2009	**86,392**

The principal trading subsidiaries are listed on page 97.

Notes to the Financial Statements
continued

13 DEFERRED TAX ASSETS AND LIABILITIES – GROUP

Recognised deferred tax assets and liabilities
Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2009 £000	2008 £000	**2009 £000**	2008 £000	**2009 £000**	2008 £000
Property, plant and equipment	**–**	–	**(3,976)**	(3,698)	**(3,976)**	(3,698)
Intangible assets	**52**	46	**(241)**	(204)	**(189)**	(158)
Employee benefits	**6,350**	4,009	**–**	–	**6,350**	4,009
Other items	**2,546**	1,363	**–**	–	**2,546**	1,363
Tax assets/(liabilities)	**8,948**	5,418	**(4,217)**	(3,902)	**4,731**	1,516
Set-off of tax	**(4,217)**	(3,902)	**4,217**	3,902	**–**	–
	4,731	1,516	**–**	–	**4,731**	1,516

Movement in deferred tax during the year

	1 January 2009 £000	**Recognised in income £000**	**Recognised in equity £000**	**31 December 2009 £000**
Property, plant and equipment	**(3,698)**	**(278)**	**–**	**(3,976)**
Intangible assets	**(158)**	**(31)**	**–**	**(189)**
Employee benefits	**4,009**	**(450)**	**2,791**	**6,350**
Other items	**1,363**	**1,111**	**72**	**2,546**
	1,516	**352**	**2,863**	**4,731**

Movement in deferred tax during the prior year

	1 January 2008 £000	Recognised in income £000	Recognised in equity £000	31 December 2008 £000
Property, plant and equipment	(3,836)	138	–	(3,698)
Intangible assets	496	(654)	–	(158)
Employee benefits	4,155	(1,012)	866	4,009
Other items	1,291	72	–	1,363
	2,106	(1,456)	866	1,516

Unrecognised deferred tax assets and liabilities
At the balance sheet date the group has unused capital losses of £9,266,000 (2008: £9,266,000) available for offset against future chargeable gains. No deferred tax asset has been recognised in respect of this amount as the group does not anticipate incurring significant chargeable gains in the foreseeable future.

Notes to the Financial Statements
continued

13 DEFERRED TAX ASSETS AND LIABILITIES – COMPANY

Recognised deferred tax assets and liabilities
Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2009 £000	2008 £000	**2009 £000**	2008 £000	**2009 £000**	2008 £000
Property, plant and equipment	**–**	–	**(3,348)**	(2,865)	**(3,348)**	(2,865)
Employee benefits	**6,067**	3,594	**–**	–	**6,067**	3,594
Cash flow hedge	**63**	–	**–**	–	**63**	–
Other items	**987**	712	**–**	–	**987**	712
Tax assets/(liabilities)	**7,117**	4,306	**(3,348)**	(2,865)	**3,769**	1,441
Set–off of tax	**(3,348)**	(2,865)	**3,348**	2,865	**–**	–
	3,769	1,441	**–**	–	**3,769**	1,441

Movement in deferred tax during the year

	1 January 2009 £000	**Recognised in income £000**	**Recognised in equity £000**	**31 December 2009 £000**
Property, plant and equipment	**(2,865)**	**(483)**	**–**	**(3,348)**
Employee benefits	**3,594**	**(540)**	**3,013**	**6,067**
Cash flow hedge	**–**	**–**	**63**	**63**
Other items	**712**	**275**	**–**	**987**
	1,441	**(748)**	**3,076**	**3,769**

Movement in deferred tax during the prior year

	1 January 2008 £000	Recognised in income £000	Recognised in equity £000	31 December 2008 £000
Property, plant and equipment	(2,858)	(7)	–	(2,865)
Employee benefits	3,614	(873)	853	3,594
Other items	676	36	–	712
	1,432	(844)	853	1,441

Unrecognised deferred tax assets and liabilities
At the balance sheet date the company has unused capital losses of 9,266,000 (2008: £9,266,000) available for offset against future chargeable gains. No deferred tax asset has been recognised in respect of this amount as the company does not anticipate incurring significant chargeable gains in the foreseeable future.

Notes to the Financial Statements
continued

14 INVENTORIES

	Group 2009 £000	Group 2008 £000	Company 2009 £000	Company 2008 £000
Finished goods and goods held for resale	**99,637**	107,597	**–**	–

Cost of sales consists of the following:

	Group 2009 £000	Group 2008 £000	Company 2009 £000	Company 2008 £000
Material cost	**366,761**	375,955	**–**	–
Processing cost	**3,450**	4,133	**–**	–
Other	**1,322**	2,582	**–**	–
	371,533	382,670	**–**	–

15 TRADE AND OTHER RECEIVABLES

	Group 2009 £000	Group 2008 £000	Company 2009 £000	Company 2008 £000
Trade receivables	**79,104**	81,696	**–**	–
Prepayments and accrued income	**3,869**	4,559	**66**	132
Other receivables	**18,176**	19,687	**267**	144
Amounts due from subsidiary undertakings	**–**	–	**26,820**	26,036
	101,149	105,942	**27,153**	26,312

£2,493,000 (2008: £2,359,000) was recognised as an impairment loss in the Consolidated Income Statement in respect of trade receivables.

The impairment loss is attributable to the geographical segments as follows:

	2009 £000	2008 £000
UK	**2,107**	2,022
Continental Europe	**386**	337
	2,493	2,359

Notes to the Financial Statements
continued

16 CASH, CASH EQUIVALENTS AND BANK OVERDRAFTS

	Group		Company	
	2009	2008	**2009**	2008
	£000	£000	**£000**	£000
Cash and cash equivalents per balance sheet	**45,737**	35,193	**27,473**	46,048
Bank overdrafts	**(758)**	–	**–**	–
Cash and cash equivalents per cash flow statements	**44,979**	35,193	**27,473**	46,048

17 ASSETS HELD FOR SALE

	Group		Company	
	2009	2008	**2009**	2008
	£000	£000	**£000**	£000
Assets classified as held for sale:				
Property, plant and equipment	**2,275**	–	**1,387**	–

At the year end the group held freehold properties in Leeds, UK, and Zutphen, the Netherlands, that were being actively marketed for sale and were expected to be disposed of during 2010. These properties became surplus to the group's requirements following the occupying businesses relocation to new purpose built facilities in 2008 and 2009 respectively.

During the year impairment losses of £1,211,000 were recognised on the remeasurement of these assets to the lower of their carrying amount and their fair value less costs to sell. These impairment losses are included in the income statement within administrative expenses (2008: £nil). Both properties were disposed of for their revised carrying value subsequent to the year end.

The Leeds and Zutphen property form part of the properties, plant and equipment reported under unallocated assets in note 2 as it is primarily a group activity to hold and maintain the properties.

18 OTHER INTEREST-BEARING LOANS AND BORROWINGS

This note provides information about the contractual terms of the group's and company's interest-bearing loans and borrowings. For more information about the group's and company's exposure to interest rate and foreign currency risk, see note 23.

	Group		Company	
	2009	2008	**2009**	2008
	£000	£000	**£000**	£000
Current liabilities				
Interest bearing loan	**900**	4,506	**–**	–
	900	4,506	**–**	–
Non-current liabilities				
Interest bearing loans	**34,392**	30,000	**30,000**	30,000
	34,392	30,000	**30,000**	30,000

18 OTHER INTEREST–BEARING LOANS AND BORROWINGS continued

Included within the interest bearing loans is an amount directly attributable to borrowing costs of £113,000 (2008: £nil).

The group has undrawn borrowing facilities expiring in one year or less which, at 31 December 2009, amounted to £44,465,000 (2008: £55,010,000). The facility conditions for drawdown had been met during the period. The borrowing is unsecured and there is a cross guarantee in place between the company and its UK subsidiaries. There is a downstream guarantee from the company in relation to its borrowing facility in the Netherlands.

The undrawn borrowing facilities are as follows:

	Interest rate %	2009 £000	Interest rate %	2008 £000
UK	2.48	35,000	1.50	45,000
Netherlands	1.78	1,333	3.75	2,262
France	1.31	5,017	3.25	4,350
Switzerland	1.70	3,115	1.75	3,398
		44,465		55,010

All the borrowing facilities above bear interest at floating rates. The Swiss facility may be drawn as an overdraft or fixed rate loan with different terms depending on length of time and amount.

19 TRADE AND OTHER PAYABLES

	Group		Company	
	2009 £000	2008 £000	2009 £000	2008 £000
Trade payables	106,494	106,228	52	198
Taxation and social security	10,717	10,466	1,718	1,416
Non–trade payables and accrued expenses	25,761	25,748	6,008	5,167
Amounts due to subsidiary undertakings	–	–	33,403	32,524
Derivative liabilities used for hedging:				
Other derivatives at fair value	20	79	–	–
Designated hedges	224	848	224	848
	143,216	143,369	41,405	40,153

Included within non-trade payables and accrued expenses is an amount of £131,000 for accrued interest on unsecured bank loans (2008: £151,000).

The group's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 23.

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS

Pension plans
During the year, the group operated a UK and Swiss defined benefit plan and defined contribution plans in the UK, France and the Netherlands. The Headlam Group plc Staff Retirement Benefits Scheme is the principal defined benefit plan which provides benefits to UK employees that have been admitted into the scheme. The scheme is self-administered and its assets are held independently of the company's finances. The scheme is funded partly by contributions from members and partly by contributions from the company at rates advised by professionally qualified actuaries. The latest actuarial valuation was carried out as at 31 March 2008 using the projected unit method. The main annual rate assumptions used by the actuary were, increase in salaries 4.7%, increase of pensions in payment 3.2%, discount rate before retirement 6.5%, discount rate after retirement 4.75% and inflation 3.2%. Assets were taken at their audited market value at the valuation date. This valuation also used revised mortality assumptions which, take account of the characteristics of plan members and include a greater allowance for future increases in longevity compared with the assumptions previously adopted.

Included within the total staff costs as disclosed in note 4 are costs relating to the group's defined contribution plans. The pension cost for the year represents contributions payable by the group to the plans and amounted to £1,524,000 (2008: £1,564,000). Contributions amounting to £118,000 (2008: £108,000) in respect of December 2009 payroll were paid in January 2010.

The total group cost of operating the plans during the year was £2,817,000 (2008: £3,195,000) and, at 31 December 2009, there was an amount of £336,000 (2008: £290,000) owed to the plans, being employer and employee contributions due for December 2009, which was paid in January 2010.

In the UK there is no contractual agreement or stated group policy for allocating the net defined benefit liability between the participating subsidiaries and as such the full deficit is recognised by the company, which is the sponsoring employer. The participating subsidiary companies have recognised a cost equal to contributions payable for the period as advised by a professionally qualified actuary. The company recognises a cost equal to its contributions payable for the period net of amounts recharged in relation to the group deficit to the participating subsidiary companies.

	Group		Company	
	2009 £000	2008 £000	**2009 £000**	2008 £000
Present value of funded defined benefit obligations	**(88,253)**	(69,441)	**(81,412)**	(62,443)
Fair value of plan assets	**65,803**	55,139	**59,583**	49,534
Net obligations	**(22,450)**	(14,302)	**(21,829)**	(12,909)
Recognised liability for defined benefit obligations	**(22,450)**	(14,302)	**(21,829)**	(12,909)
Other long term employee benefits (note 21)	**(309)**	(342)	**–**	–
Total employee benefits	**(22,759)**	(14,644)	**(21,829)**	(12,909)
Split:				
Current liabilities	**(2,506)**	(2,428)	**(2,506)**	(2,428)
Non-current liabilities	**(20,253)**	(12,216)	**(19,323)**	(10,481)
Total employee benefits	**(22,759)**	(14,644)	**(21,829)**	(12,909)

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS continued

Pension plans continued
Following the actuarial valuation of the Headlam Group plc Staff Retirement Benefits Scheme as at 31 March 2008, a recovery plan was agreed between the Trustees of the scheme and the company to fund the deficit. In accordance with the recovery plan, payments were made to the scheme during 2009 of £2,419,000 which, in accordance with the recovery plan, increase to £2,506,000 in 2010. It was agreed that recovery payments, which commenced on 1 January 2009 and will cease on 31 March 2018, were to increase by 3.2% each year. The next actuarial valuation is due at 31 March 2011 for the UK plan.

In addition to the recovery payments, company contributions as at the date of the last valuation have been fixed at 24.7% of pensionable salaries at that date, with no allowance made in respect of subsequent leavers. This represented an additional contribution amounting to £188,000 during 2009.

The group and company expect to pay regular ongoing contributions of approximately £3,994,000 (2008: £3,988,000) to defined benefit plans in the next financial year.

Movements in present value of defined benefit obligation

	Group		Company	
	2009 £000	2008 £000	**2009 £000**	2008 £000
At 1 January	**69,441**	71,350	**62,443**	66,953
Current service cost	**1,268**	1,461	**868**	1,271
Interest cost	**4,202**	4,075	**4,013**	3,925
Actuarial losses/(gains)	**16,125**	(7,553)	**16,320**	(7,660)
Benefits paid	**(2,457)**	(2,422)	**(2,480)**	(2,294)
Contributions by members	**357**	355	**223**	248
Past service costs	**25**	–	**25**	–
Effect of movements in foreign exchange	**(708)**	2,175	**–**	–
At 31 December	**88,253**	69,441	**81,412**	62,443

Movements in fair value of plan assets

	Group		Company	
	2009 £000	2008 £000	**2009 £000**	2008 £000
At 1 January	**55,139**	60,308	**49,534**	56,098
Expected return on plan assets	**3,061**	3,905	**2,859**	3,713
Actuarial gains/(losses)	**6,083**	(11,798)	**5,559**	(10,785)
Contributions by employer	**4,078**	2,706	**3,888**	2,554
Contributions by members	**357**	355	**223**	248
Benefits paid	**(2,457)**	(2,422)	**(2,480)**	(2,294)
Effect of movements in foreign exchange	**(458)**	2,085	**–**	–
At 31 December	**65,803**	55,139	**59,583**	49,534

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS continued

Pension plans continued
Expense recognised in the income statement

	Group 2009 £000	Group 2008 £000
Current service cost	**1,268**	1,461
Past service cost	**25**	–
Interest on defined benefit plan obligation	**4,202**	4,075
Expected return on defined benefit plan assets	**(3,061)**	(3,905)
Total	**2,434**	1,631

The expense is recognised in the following line items in the Consolidated Income Statement:

	Group 2009 £000	Group 2008 £000
Administrative expenses	**1,293**	1,461
Net financing costs	**1,141**	170
	2,434	1,631

Actuarial gains and losses in the Statement of Comprehensive Income:

	Group 2009 £000	Group 2008 £000
Actuarial (losses)/gains on defined benefit obligation	**(16,125)**	7,553
Actuarial gain/(losses) on plan assets	**6,083**	(11,798)
	(10,042)	(4,245)

Cumulative actuarial gains and losses reported in the Statement of Comprehensive Income (formerly known as the Statement of Recognised Income and Expense) since 1 January 2004, the transition date to IFRS, are £15,785,000 (2008: £5,743,000). Cumulative actuarial gains and losses reported in the company's Statement of Comprehensive Income are £15,170,000 (2008: £4,409,000).

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS continued

Pension plans continued

The fair value of the plan assets and the return on those assets were as follows:

	Group		Company	
	2009 £000	2008 £000	**2009 £000**	2008 £000
Equities	**36,107**	28,202	**34,844**	27,227
Government debt	**15,995**	15,438	**15,995**	15,438
Corporate bonds	**7,171**	5,782	**4,198**	2,856
Annuities	**4,371**	3,909	**4,371**	3,909
Other	**2,159**	1,808	**175**	104
	65,803	55,139	**59,583**	49,534
Actual return on plan assets	**9,144**	(7,837)	**8,418**	(7,072)

The expected rates of return on plan assets are determined by reference to relevant indices. The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the plan's investment portfolio.

	Group		Company	
	2009 %	2008 %	**2009 %**	2008 %
Discount rate	**5.6**	6.1	**5.8**	6.5
Future salary increases	**5.0**	4.2	**5.3**	4.5
Future pension increases	**3.5**	2.7	**3.8**	3.0
Inflation rate	**3.6**	2.8	**3.8**	3.0
Expected rate of return on plan assets	**6.1**	5.5	**6.3**	5.7
Mortality table assumptions:				
UK pre-retirement	**AC00 (Ultimate) table**	AC00 (Ultimate) table	**AC00 (Ultimate) table**	AC00(Ultimate) table
UK post-retirement - future-pensioners	**103%(M)/110%(F) of the PCA00 tables with medium cohort projections**	103%(M)/110%(F) of the PCA00 tables with medium cohort projections	**103%(M)/110%(F) of the PCA00 tables with medium cohort projections**	103%(M)/110%(F) of the PCA00 tables with medium cohort projections
UK post-retirement - current pensioners	**103%(M)/110%(F) of the PCA00 tables with medium cohort projections**	103%(M)/110%(F) of the PCA00 tables with medium cohort projections	**103%(M)/110%(F) of the PCA00 tables with medium cohort projections**	103%(M)/110%(F) of the PCA00 tables with medium cohort projections
Swiss scheme	**EVK 2000**	EVK 2000	**–**	–

	Group		Company	
	2009	2008	**2009**	2008
Non-pensioner male	**23.3**	23.3	**23.3**	23.3
Pensioner male	**21.3**	21.3	**21.3**	21.3
Non-pensioner female	**25.2**	25.1	**25.2**	25.1
Pensioner female	**23.3**	23.2	**23.3**	23.2

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS continued

Pension plans continued

History of plans
The history of the plans for the current and prior periods is as follows:

Balance sheet

Group	2009 £000	2008 £000	2007 £000	2006 £000	2005 £000
Present value of defined benefit obligation	**(88,253)**	(69,441)	(71,350)	(73,160)	(64,750)
Fair value of plan assets	**65,803**	55,139	60,308	56,220	44,524
Deficit	**(22,450)**	(14,302)	(11,042)	(16,940)	(20,226)

Company	2009 £000	2008 £000	2007 £000	2006 £000	2005 £000
Present value of defined benefit obligation	**(81,412)**	(62,443)	(66,953)	(69,736)	(64,750)
Fair value of plan assets	**59,583**	49,534	56,098	52,704	44,524
Deficit	**(21,829)**	(12,909)	(10,855)	(17,032)	(20,226)

Experience adjustments

Group	2009 £000	2008 £000	2007 £000	2006 £000	2005 £000
On plan liabilities	**16,121**	(7,553)	(4,493)	1,688	6,711
On plan assets	**6,083**	(11,798)	507	1,518	4,134
As a percentage of plan liabilities	**18.3%**	(10.9%)	(6.3%)	2.3%	10.4%
As a percentage of plan assets	**9.2%**	(21.4%)	0.8%	2.7%	9.3%

Company	2009 £000	2008 £000	2007 £000	2006 £000	2005 £000
On plan liabilities	**16,320**	(7,660)	(4,989)	1,664	6,711
On plan assets	**5,559**	(10,785)	313	1,403	4,134
As a percentage of plan liabilities	**20.0%**	(12.3%)	(7.5%)	2.4%	10.4%
As a percentage of plan assets	**9.3%**	(21.8%)	0.6%	2.7%	9.3%

20 EMPLOYEE BENEFITS continued

Share-based payments – Group and company

Executive directors and executive management currently participate in executive share option schemes. The option price may not be less than the greater of the mid-market value of the group's shares at the time when the options were granted or the nominal value. Options granted under the 1998 Inland Revenue approved scheme are normally exercisable between the third and tenth anniversaries of their date of grant, subject to the movement of the group's basic earnings per share exceeding RPI over the relevant period.

Options granted under the 1998 unapproved scheme are normally exercisable between the third and seventh anniversaries of their date of grant. Awards are subject to the movement of the group's basic earnings per share exceeding RPI between 3% and 5% per annum respectively over the relevant period.

Additionally, the group operates a savings related share option scheme ("sharesave scheme") which is open to employees subject to eligibility criteria determined by the directors prior to each option grant. The most recent grant was on 19 May 2009 when employees with over one month's service were invited to participate.

The group also operates a 2008 HMRC approved scheme, a 2008 unapproved scheme, the Headlam Group Performance Share Plan 2008 and the Headlam Group Co-Investment Plan 2008. The group has not yet implemented any of these schemes or plans. Further details of these schemes and plans are given in the Remuneration Report on page 38.

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS continued

Share-based payments – Group and company continued
The terms and conditions of the grants are as follows, whereby all options are settled by physical delivery of shares:

Grant date/employees entitled	Number of instruments 2009	2008	Vesting conditions	Contractual life of options
Approved 1998 scheme grant to key management 10 January 2001	–	10,000	Movement of the group's basic earnings per share exceeding RPI over the relevant period	10/01/04 – 10/01/11
Approved 1998 scheme grant to key management 14 April 2003	**46,404**	46,404	Movement of the group's basic earnings per share exceeding RPI over the relevant period	14/04/06 – 14/04/13
Unapproved 1998 scheme grant to key management 14 April 2003	**2,596**	2,596	Movement of the group's basic earnings per share exceeding RPI over the relevant period	14/04/06 – 14/04/10
Unapproved 1998 scheme grant to key management 22 August 2005	**1,242,864**	1,242,864	Movement of the group's basic earnings per share exceeding RPI by 3%-5% pa over the relevant period	22/08/08 – 22/08/12
Approved 1998 scheme granted to key management 22 August 2005	**57,136**	57,136	Movement of the group's basic earnings per share exceeding that of RPI by 3% pa over the relevant period	22/08/08 – 22/08/15
Three year sharesave scheme granted to other employees 25 May 2006	–	95,278	Continuous service	01/07/09 – 01/01/10
Five year sharesave scheme granted to other employees 25 May 2006	**45,152**	83,532	Continuous service	01/07/11 – 01/01/12
Three year sharesave scheme granted to other employees 8 May 2008	**73,098**	267,740	Continuous service	01/07/11 – 01/01/12
Five year sharesave scheme granted to other employees 8 May 2008	**57,740**	310,305	Continuous service	01/07/13 – 01/01/14
Three year sharesave scheme granted to other employees 19 May 2009	**481,635**	–	Continuous service	01/07/12 – 01/01/13
Five year sharesave scheme granted to other employees 19 May 2009	**400,441**	–	Continuous service	01/07/14 – 01/01/15
Total share options	**2,407,066**	2,115,855		

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS continued

Share-based payments – Group and company continued

The number and weighted average exercise prices of share options are as follows:

	Weighted average exercise price 2009	Number of options 2009	Weighted average exercise price 2008	Number of options 2008
Outstanding at the beginning of the year	**379.5**	**2,115,855**	370.1	2,114,930
Exercised during the year	**–**	**–**	197.5	(380,306)
Granted during the year	**222.2**	**895,909**	303.2	626,609
Lapsed during the year	**320.1**	**(604,698)**	335.5	(245,378)
Outstanding at the end of the year	**336.6**	**2,407,066**	379.5	2,115,855
Exercisable at the end of the year	**411.4**	**1,357,234**	410.2	1,362,985

There were no options exercised during the year, the weighted average share price for options exercised during 2008 was 396.7p.

The options outstanding at the year end have an exercise price in the range of 215.0p to 420.0p and a weighted average contractual life of 4.7 years.

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of the fair value of the services received is measured using the Black-Scholes option pricing model.

It is expected that the options will be exercised as soon as they reach maturity.

There are no market conditions associated with the share option grants.

The expected volatility is based on historic volatility calculated over the weighted average remaining life of the share options.

Details of share options granted during 2009 are shown below:

2009	3 year options	5 year options
Number of options	495,468	400,441
Fair value at measurement date	76.2p	67.4p
Share price at 31 December	300.3p	300.3p
Exercise price	222.2p	222.2p
Expected volatility (expressed as weighted average volatility used in the modelling under the Black-Scholes model)	48.6%	42.2%
Option life (expressed as weighted average life used in the modelling under the Black-Scholes model)	3 years	5 years
Expected dividends	7.6%	7.6%
Risk-free interest rate (based on UK Gilts)	2.1%	2.8%

Notes to the Financial Statements
continued

20 EMPLOYEE BENEFITS continued

Share-based payments – Group and company continued
Details of share options granted during 2008 are shown below:

2008	3 year options	5 year options
Fair value at measurement date	117.7p	108.4p
Share price at 31 December	210.5p	210.5p
Exercise price	303.2p	303.2p
Expected volatility (expressed as weighted average volatility used in the modelling under the Black-Scholes model)	47.2%	40.4%
Option life (expressed as weighted average life used in the modelling under the Black-Scholes model)	3 years	5 years
Expected dividends	6.2%	6.2%
Risk-free interest rate (based on UK Gilts)	4.3%	4.3%

The total expenses recognised for the year arising from share based payments are as follows:

	Group		Company		Subsidiaries	
	2009 £000	2008 £000	**2009 £000**	2008 £000	**2009 £000**	2008 £000
Share options granted in 2005 under the approved 1998 scheme	**–**	11	**–**	4	**–**	7
Share options granted in 2005 under the unapproved 1998 scheme	**–**	236	**–**	119	**–**	117
Share options granted in 2006 under the SAYE 3 year scheme	**30**	38	**1**	1	**29**	37
Share options granted in 2006 under the SAYE 5 year scheme	**36**	19	**–**	–	**36**	19
Share options granted in 2008 under the SAYE 3 year scheme	**101**	74	**–**	2	**101**	72
Share options granted in 2008 under the SAYE 5 year scheme	**67**	48	**–**	2	**67**	46
Share options granted in 2009 under the SAYE 3 year scheme	**63**	–	**1**	–	**62**	–
Share options granted in 2009 under the SAYE 5 year scheme	**19**	–	**1**	–	**18**	–
Total expense recognised	**316**	426	**3**	128	**313**	298

Notes to the Financial Statements
continued

21 OTHER LONG TERM EMPLOYEE BENEFITS – GROUP

During the year, the group operated an employment indemnity scheme in connection with a foreign subsidiary undertaking to provide for lump sum cash payments due to employees retiring on their normal retirement date. The present retirement indemnity obligation at 31 December 2009 is £309,000 (2008: £342,000).

22 CAPITAL AND RESERVES – GROUP AND COMPANY

Share capital

	Ordinary shares	
	2009	2008
Number of shares		
On issue at 1 January and 31 December – fully paid	**85,363,743**	85,363,743

	2009 £000	2008 £000
Allotted, called up and fully paid		
Ordinary shares of 5p each	**4,268**	4,268
	4,268	4,268
Shares classified as liabilities	**–**	–
Shares classified in shareholders funds	**4,268**	4,268
	4,268	4,268

At 31 December 2009, there were 2,248,647 shares held in treasury. Dividends are not payable on these shares and they are excluded from the calculation of earnings per share. The shares held in treasury represent 2.6% of the issued share capital with a nominal value of £112,000.

In the period from 31 December 2009 to 19 March 2010 no shares have been purchased by the company.

Ordinary shares
The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the company.

Dividends

	2009 £000	2008 £000
Interim dividend for 2008 of 5.60p paid 2 January 2009	**4,649**	–
Final dividend for 2008 of 14.10p paid 1 July 2009	**11,705**	–
Interim dividend for 2007 of 5.35p paid 2 January 2008	**–**	4,454
Final dividend for 2007 of 17.75p paid 1 July 2008	**–**	14,728
	16,354	19,182

The final proposed dividend of 7.30p per share (2008:14.10p per share) will not be provided for until authorised by shareholders at the forthcoming AGM.

Interim dividends of 3.70p per share (2008: 5.60p per share) are provided for when the dividend is paid.

Notes to the Financial Statements
continued

22 CAPITAL AND RESERVES – GROUP AND COMPANY continued

The total value of dividends proposed but not recognised at 31 December 2009 is £9,132,000 (2008: £16,354,000).

Reserves

Other reserves
Other reserves as disclosed on the balance sheet comprise the capital redemption reserve, translation reserve, cash flow hedging reserve and treasury reserve. For the company this also includes a special reserve.

Capital redemption reserve
The capital redemption reserve represents the nominal value of shares repurchased and cancelled during 2007.

Translation reserve
The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Cash flow hedging reserve
The cash flow hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments relating to hedged transactions that have not yet occurred.

Treasury Reserve
The treasury reserve compromises the cost of the company's shares held by the group.

Special Reserve
The special reserve arose on the issuance of shares in connection with acquisitions made by the company in earlier years.

23 FINANCIAL INSTRUMENTS

The main financial risks arising in the normal course of the group's business are credit risk, liquidity risk, and market risks arising from interest rate risk and foreign currency risk. This note presents information about the group's exposure to each of the above risks, the group's objectives, policies and processes for measuring and managing risks and the group's management of capital. Further quantitative disclosures are included throughout these financial statements.

Credit risk
Credit risk is the risk of financial loss to the group if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the group's trade receivables.

The company and group have a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all new customers requiring credit cover over £1,000 and these are frequently reviewed by management to limit exposure. Businesses must obtain central approval for credit limits in excess of £10,000. The group does not require collateral in respect of financial assets.

At the balance sheet date, there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

23 FINANCIAL INSTRUMENTS continued

Credit risk continued

The carrying amount of financial assets at the balance sheet date was:

	Group 2009 £000	Group 2008 £000	Company 2009 £000	Company 2008 £000
Trade and other receivables (note 15)	**101,149**	105,942	**27,153**	26,312
Cash and cash equivalents (note 16)	**45,737**	35,193	**27,473**	46,048
	146,886	141,135	**54,626**	72,360

The fair values of the above financial assets at both 31 December 2009 and 2008, are deemed to approximate to carrying value due to the short term maturity of the instruments.

The maximum exposure to credit risk for trade receivables at the balance sheet date by geographic region was:

	Group 2009 £000	Group 2008 £000	Company 2009 £000	Company 2008 £000
UK	**63,231**	63,774	**–**	–
Continental Europe	**15,873**	17,922	**–**	–
	79,104	81,696	**–**	–

The ageing of trade receivables at the balance sheet date was:

	2009 Gross £000	2009 Impairment £000	2008 Gross £000	2008 Impairment £000
Not past due	**74,760**	**–**	77,054	–
Past due 0–30 days	**3,718**	**(505)**	3,410	–
Past due 31–120 days	**3,427**	**(2,296)**	4,310	(3,078)
	81,905	**(2,801)**	84,774	(3,078)

The company had trade receivables of £nil (2008:£nil).

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

	Group 2009 £000	Group 2008 £000	Company 2009 £000	Company 2008 £000
Balance at 1 January	**3,078**	1,873	**–**	–
Impairment loss	**2,493**	2,359	**–**	–
Amounts provided	**(2,690)**	(1,446)	**–**	–
Effect of movements in foreign exchange	**(80)**	292	**–**	–
Balance at 31 December	**2,801**	3,078	**–**	–

Notes to the Financial Statements
continued

23 FINANCIAL INSTRUMENTS continued

Credit risk continued
Based on historic default rates, the group believes that no general impairment allowance is necessary in respect of trade receivables, however, the group provides fully for specific debts when required. During the year the group's impairment loss as a percentage of revenue amounted to 0.47% (2008: 0.42%).

Liquidity risk
Liquidity risk is the risk that the group will not be able to meet its financial obligations as they fall due. The group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, with sufficient headroom to cope with abnormal market conditions. As at 31 December 2009 cash and cash equivalents covered the amounts of borrowings maturing in the next twelve months with a net positive liquidity of £44,079,000 (2008: £30,687,000). Details of the total facilities that the group has access to are given in note 18.

The following are the contractual maturities of financial liabilities:

31 December 2009 Group	**Carrying amount £000**	**Contractual cash flows £000**	**1 year or less £000**	**1–2 years £000**	**2–5 years £000**	**More than 5 years £000**
Non-derivative financial liabilities						
Bank overdraft	**758**	**(768)**	**(768)**	**–**	**–**	**–**
Unsecured bank loans	**35,292**	**(37,166)**	**(1,404)**	**(714)**	**(31,588)**	**(3,460)**
Trade and other payables	**142,972**	**(142,972)**	**(142,972)**	**–**	**–**	**–**
Derivative financial liabilities						
Interest rate swaps used for hedging	**224**	**(224)**	**(224)**	**–**	**–**	**–**
Forward exchange contracts used for hedging	**20**	**(20)**	**(20)**	**–**	**–**	**–**
	179,266	**(181,150)**	**(145,388)**	**(714)**	**(31,588)**	**(3,460)**

31 December 2008 Group	Carrying amount £000	Contractual cash flows £000	1 year or less £000	1–2 years £000	2-5 years £000
Non-derivative financial liabilities					
Unsecured bank loans	34,506	(37,171)	(5,388)	(713)	(31,070)
Trade and other payables	142,442	(142,442)	(142,442)	–	–
Derivative financial liabilities					
Interest rate swaps used for hedging	848	(848)	(848)	–	–
Forward exchange contracts used for hedging	79	(79)	(79)	–	–
	177,874	(180,540)	(148,757)	(713)	(31,070)

Notes to the Financial Statements
continued

23 FINANCIAL INSTRUMENTS continued

Liquidity risk continued

31 December 2009 Company	**Carrying amount £000**	**Contractual cash flows £000**	**1 year or less £000**	**1–2 years £000**	**2–5 years £000**
Non-derivative financial liabilities					
Unsecured bank loans	**30,000**	**(30,913)**	**(365)**	**(365)**	**(30,182)**
Trade and other payables	**41,181**	**(41,181)**	**(41,181)**	**–**	**–**
Derivative financial liabilities					
Interest rate swaps used for hedging	**224**	**(224)**	**(224)**	**–**	**–**
	71,405	**(72,318)**	**(41,770)**	**(365)**	**(30,182)**

31 December 2008 Company	Carrying amount £000	Contractual cash flows £000	1 year or less £000	1–2 years £000	2–5 years £000
Non-derivative financial liabilities					
Unsecured bank loans	30,000	(32,496)	(713)	(713)	(31,070)
Trade and other payables	39,305	(39,305)	(39,305)	–	–
Derivative financial liabilities					
Interest rate swaps used for hedging	848	(848)	(848)	–	–
	70,153	(72,649)	(40,866)	(713)	(31,070)

The value of the group's financial liabilities as detailed above at 31 December 2009 and 2008 were not materially different to the carrying value. Fair values were calculated using market rates, where available. Where market values are not available, fair values have been estimated by discounting expected future cash flows using prevailing interest rate curves. Amounts denominated in foreign currencies are valued at the exchange rate prevailing at the balance sheet date.

Notes to the Financial Statements
continued

23 FINANCIAL INSTRUMENTS continued

Liquidity risk continued
The table below sets out the group's accounting classification of each class of financial assets and liabilities at 31 December 2009 and 2008.

31 December 2009	Available for sale £000	Designated hedges £000	Other derivatives at fair value £000	Amortised cost £000	Total carrying value £000
Cash and cash equivalents	45,737	–	–	–	45,737
Bank overdrafts	–	–	–	(758)	(758)
Borrowings due within one year	–	–	–	(900)	(900)
Borrowings due after one year	–	–	–	(34,392)	(34,392)
Trade payables	–	–	–	(106,494)	(106,494)
Trade receivables	–	–	–	79,104	79,104
Derivative liabilities	–	(224)	(20)	–	(244)
	45,737	(224)	(20)	(63,440)	(17,947)

31 December 2008	Available for sale £000	Designated hedges £000	Other derivatives at fair value £000	Amortised cost £000	Total carrying value £000
Cash and cash equivalents	35,193	–	–	–	35,193
Borrowings due within one year	–	–	–	(4,506)	(4,506)
Borrowings due after one year	–	–	–	(30,000)	(30,000)
Trade payables	–	–	–	(106,228)	(106,228)
Trade receivables	–	–	–	81,696	81,696
Derivative liability	–	(848)	(79)	–	(927)
	35,193	(848)	(79)	(59,038)	(24,772)

Under IAS 39, all derivative financial instruments not in a hedge relationship are derivatives at fair value through the consolidated Income Statement. The group does not use derivatives for speculative purposes. All transactions in derivative financial instruments are undertaken to manage the risks arising from underlying business activities.

Notes to the Financial Statements
continued

23 FINANCIAL INSTRUMENTS continued

Interest rate risk
The company and group are exposed to interest rate fluctuations on its borrowings and cash deposits. Borrowings are principally held in sterling and euro's at both fixed and floating rates, deposits are in sterling, euro's and Swiss francs at floating rates.

Floating rate borrowings are linked to the London Interbank Offered Rate. The group adopts a policy of maintaining a portion of its borrowings at fixed interest rate and reviewing the balance of the floating rate exposure to ensure that if interest rates rise the effect on the group's income statement is manageable. In accordance with this policy, and in order to manage it's exposure to interest rates, the group entered into two interest rate swaps in 2008 to fix £30 million of its sterling denominated borrowings. The first interest rate swap matured in October 2009 and the second is due to mature in April 2010. These interest rate swaps have been designated as a hedging instrument and accounted for as a cash flow hedge in accordance with the requirements of IAS 39.

The fair values of these interest rate swaps are included in the balance sheet as a £224,000 derivative liability (2008: £848,000).

At the reporting date the interest rate profile of the group's interest–bearing financial instruments was:

	Group Carrying amount		Company Carrying amount	
	2009 £000	2008 £000	**2009 £000**	2008 £000
Variable rate instruments				
Financial assets	**45,737**	35,193	**27,473**	46,048
Financial liabilities	**(36,050)**	(34,506)	**(30,000)**	(30,000)
	9,687	687	**(2,527)**	16,048

There were no fixed rate instruments held by the group at 31 December 2009 (2008 : £nil).

Sensitivity analysis
A change of 100 basis points in the interest rates at the reporting date would have increased/(decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis as that used for 2008.

	Group				Group			
	Profit or loss		Equity		Profit or loss		Equity	
	100bp increase £000	**100bp decrease £000**	**100bp increase £000**	**100bp decrease £000**	**100bp increase £000**	**100bp decrease £000**	**100bp increase £000**	**100bp decrease £000**
31 December 2009								
Variable rate instruments	**197**	**(197)**	**–**	**–**	**75**	**(75)**	**–**	**–**
31 December 2008								
Variable rate instruments	307	(307)	–	–	460	(460)	–	–

Notes to the Financial Statements
continued

23 FINANCIAL INSTRUMENTS continued

Foreign currency risk
The group and company are exposed to movements in currency exchange rates arising from transaction currency cash flows and the translation of the results and net assets of overseas subsidiary operations. The currencies giving rise to this risk are primarily the euro and Swiss franc.

The group and company uses forward exchange contracts to hedge its foreign currency transactional risk. A future foreign currency contract would be entered into where there was a known requirement for the currency due to planned imports that are not invoiced in sterling. These forward exchange contracts would have a maturity of less than one year after the balance sheet date. The group also enters into foreign currency contracts at spot rate where the amounts are not frequent or material. Gains and losses on currency contracts recognised as a liability as at 31 December 2009 amounted to £20,000 (2008: £79,000).

For the twelve month period to 31 December 2009, 10.0% (2008: 8.6%) of the group's operating profit was derived from overseas subsidiaries and at 31 December 2009, 22.5% (2008: 22.0%) of the group's operating assets related to overseas subsidiary operations. Hedge accounting, following the adoption of IFRS, has not been applied to these operations.

The group and company do not use derivatives other than as described above.

The group's exposure to foreign currency risk was as follows based on notional amounts:

	Group			Company		
2009	**Euro amount £000**	**Other amount £000**	**Total £000**	**Euro amount £000**	**Other amount £000**	**Total £000**
Trade and other receivables	**279**	**144**	**423**	**56**	**12**	**68**
Cash and cash equivalents	**319**	**387**	**706**	**234**	**1**	**235**
Trade and other payables	**(1,064)**	**(666)**	**(1,730)**	**–**	**–**	**–**
	(466)	**(135)**	**(601)**	**290**	**13**	**303**

	Group			Company		
2008	Euro amount £000	Other amount £000	Total £000	Euro amount £000	Other amount £000	Total £000
Trade and other receivables	57	19	76	88	19	107
Cash and cash equivalents	262	452	714	182	1	183
Trade and other payables	(1,837)	(282)	(2,119)	–	–	–
	(1,518)	189	(1,329)	270	20	290

23 FINANCIAL INSTRUMENTS continued

Sensitivity analysis
A 10 per cent weakening of sterling against the following currencies at 31 December would have increased /(decreased) profit or loss by the amounts shown below. There is no equity effect. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis as that used for 2008.

	Group		Company	
	Equity 2009 £000	Equity 2008 £000	**Equity 2009 £000**	Equity 2008 £000
Euro	**(47)**	(152)	**29**	27
Other	**(14)**	19	**1**	2

A 10 per cent strengthening of sterling against the above currencies at 31 December would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Fair values hierarchy
The financial instruments carried at fair value are categorised according to their valuation method. The different levels have been defined below:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices)
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The group has an interest rate swap used for hedging which was fair valued in accordance with level 2 for the year ended 31 December 2009 (2008: level 2) and forward currency contracts which are fair valued in accordance with level 3 (2008: level 3).

Fair values
The carrying amounts shown in the balance sheet for financial instruments are a reasonable approximation to fair value.

Trade receivables, trade payables and cash and cash equivalents – Fair values are assumed to approximate to cost due to the short term maturity of the instrument.

Borrowings, other financial assets and other financial liabilities – Where available, market values have been used to determine fair values. Where market values are not available, fair values have been estimated by discounting expected future cash flows using prevailing interest rate curves. Amounts denominated in foreign currencies are valued at the exchange rate prevailing at the balance sheet date.

Capital management
The board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The board closely monitors its shareholder base, dividend yield and earnings per share.

The board encourages employees of the group to hold the company's ordinary shares. The group operates a number of employee share option schemes. The company has acquired a number of its own shares under a share buy-back programme, some of which, have been used for issuing shares under the group's various share option incentive schemes.

In order to maintain or adjust the capital structure, the group may vary dividends payable, return capital to shareholders, issue new shares or sell assets to reduce debt.

Notes to the Financial Statements
continued

24 ACQUISITIONS OF SUBSIDIARIES

No acquisitions were made during the year ended 31 December 2009.

On 5 November 2008, a group subsidiary company acquired the trade and assets of Silvester, a supplier of residential products to independent retailers throughout the Netherlands for a cash consideration of £577,000. Since its acquisition the business has contributed profit of £60,000 to the consolidated profit for the year ended 31 December 2008 attributable to the equity shareholders. If the acquisition had occurred on 1 January 2008 group revenue would have been an estimated £559,760,000 and profit would have been an estimated £28,859,000.

On 18 March 2008, a group subsidiary company acquired the inventory and intellectual property rights of I–Floor for a cash consideration of £94,000.

	Acquiree's book value £000	Fair value adjustments £000	Acquisition amounts £000
Acquiree's net assets at the acquisition date:			
Intangible assets	–	263	263
Property, plant and equipment			
Inventories	412	–	412
Trade and other receivables	318	–	318
Trade and other payables	(267)	–	(267)
Net identifiable assets and liabilities	463	263	726
Goodwill on acquisition			–
Consideration paid			(726)
Satisfied by:			
Cash			667
Acquisition costs capitalised			59
			726
Analysis of cash flows:			
On completion			(667)
Costs of acquisition			(59)
			(726)

No goodwill has arisen on the acquisition of the trade and assets of Silvester or I Floor. The intangible assets on acquisition were attributed to customer order books.

Following acquisition, it is the group's normal practice to implement its operational and financial procedures and standard IT systems.

Furthermore, acquired businesses gain access to the group's extensive product ranges and benefit from enhanced sales and marketing investment. These changes typically enable acquired businesses to enhance the service provided to their customers and ultimately, develop and grow.

Whilst acquired customer order books are a key component at the point of acquisition, this position quickly dissipates during the post acquisition period. The dynamic and renewable nature of this class of asset is the reason the group elects to amortise it over a period of one to twenty four months, the precise period being dependant upon the size of the acquired business.

Notes to the Financial Statements
continued

25 OPERATING LEASES

The aggregate payments, for which there are commitments under non–cancellable operating leases as at the end of the year, fall due as follows:

Group	2009 Land and buildings £000	2009 Plant and machinery £000	2009 Total £000	2008 Land and buildings £000	2008 Plant and machinery £000	2008 Total £000
Less than one year	**423**	**1,153**	**1,576**	893	7,614	8,507
Between one and five years	**2,738**	**16,546**	**19,284**	3,427	13,634	17,061
More than five years	**3,406**	**17**	**3,423**	2,135	258	2,393
	6,567	**17,716**	**24,283**	6,455	21,506	27,961

Company	2009 Land and buildings £000	2009 Plant and machinery £000	2009 Total £000	2008 Land and buildings £000	2008 Plant and machinery £000	2008 Total £000
Less than one year	**18**	**7**	**25**	16	7	23
Between one and five years	**74**	**6**	**80**	65	13	78
More than five years	**1,414**	**–**	**1,414**	1,259	–	1,259
	1,506	**13**	**1,519**	1,341	20	1,360

The group leases the majority of its motor and commercial vehicles on terms that range between three and five years.

During the year ended 31 December 2009, £10,952,000 was recognised as an expense in the Consolidated Income Statement in respect of operating leases (2008: £11,201,000).

26 CAPITAL COMMITMENTS

Group
During the year ended 31 December 2009, the group entered into contracts to purchase property, plant and equipment for £225,000 (2008: £629,000). These commitments are expected to be settled in the following financial year.

Company
During the year ended 31 December 2009, the company entered into contracts to purchase property, plant and equipment for £nil (2008: £16,000).

Notes to the Financial Statements

continued

27 RELATED PARTIES

Group and Company

Identity of related parties

The group has a related party relationship with its subsidiaries and with its directors and executive officers.

Transactions with key management personnel

The group's key management personnel are the executive and non-executive directors as indentified in the Remuneration Report on page 40.

As at 31 December 2009, directors of the company and their immediate relatives controlled 1.6 per cent of the voting shares of the company (2008:1.6 per cent).

In addition to their salaries, the group also contributes to a post-employment defined benefit plan on behalf of the executive directors. Executive directors also participate in the group's share option schemes.

Non-executive directors receive a fee for their services to the board.

Other than disclosed in the Remuneration Report, there were no other transactions with key management personnel in either the current or preceeding year. The IFRS 2 cost charged to administrative expenses relating to share options of key management personnel amounted to £2,000 (2008:£116,000).

Company only

In addition to the transactions with key management personnel the company has the following transactions:

Transactions with other group companies

	Highest during the year £000	**Balance at 31 December 2009 £000**	Highest during the year £000	Balance at 31 December 2008 £000
Amounts due from subsidiary undertakings	**26,820**	**26,820**	26,036	26,036
Amounts due to subsidiary undertakings	**(33,403)**	**(33,403)**	(32,524)	(32,524)

The disclosure of the year end balance and the highest balance during the year is considered to provide a meaningful representation of transactions between the company and its subsidiaries in the year. The highest balance is generally at the start or close of the financial period since this is the time when the company levies its management charge.

Transactions reported in the income statement

	For year ended 31 December 2009 £000	For year ended 31 December 2008 £000
Rental income	**5,942**	5,453
Dividends received	**1,375**	9,586
Management charges	**1,659**	2,375
Interest income	**259**	790
Pension recharge	**236**	260

28 SUBSEQUENT EVENTS

At the year end the group held freehold properties in Leeds, UK, and Zutphen, the Netherlands, that were surplus to the group's requirements and were being actively marketed for sale. These properties were subsequently sold on 28 January 2010 and 2 March 2010 respectively.

Cash received on completion of the property in Leeds was £444,000 with a further £943,000 to be received during the next two years. Cash received on the sale of the property in Zutphen was €1,000,000.

Principal Trading Subsidiaries

	Place of incorporation
• HFD Limited	Great Britain
• MCD Group Limited	Great Britain
Headlam BV	Netherlands
LMS SA	France
• Belcolor AG	Switzerland

All of these subsidiaries are wholly owned and are principally engaged as a distributor of floorcoverings and associated products.

- These subsidiaries are owned directly by Headlam Group plc. The investment in subsidiaries comprises ordinary share capital.

Financial Record

	2005 £000	2006 £000	2007 £000	2008 £000	**2009 £000**
Trading results					
Revenue	486,653	509,899	544,718	557,296	**533,793**
Operating profit	41,498	43,941	46,013	41,722	**24,758**
Profit before net financing costs	41,498	43,941	46,013	41,722	**24,758**
Net financing costs	(658)	(383)	(841)	(1,602)	**(2,694)**
Profit on ordinary activities before tax	40,840	43,558	45,172	40,120	**22,064**
Taxation	(12,352)	(13,067)	(13,534)	(11,433)	**(6,168)**
Profit on ordinary activities after taxation	28,488	30,491	31,638	28,687	**15,896**
Shareholder value					
Paid dividend per share	16.25p	18.00p	20.15p	23.10p	**19.70p**
Proposed dividend per share	18.00p	20.15p	23.10p	19.70p	**11.00p**
Earnings per share	33.1p	35.1p	37.1p	34.5p	**19.1p**
Net assets					
Non-current assets					
Property, plant and equipment	74,640	85,032	92,097	99,741	**96,530**
Intangible assets	13,210	13,210	13,210	13,210	**13,210**
Deferred tax assets	6,796	5,517	2,106	1,516	**4,731**
	94,646	103,759	107,413	114,467	**114,471**
Current assets					
Inventories	91,160	94,217	101,491	107,597	**99,637**
Trade and other receivables	84,275	91,284	100,830	105,942	**101,149**
Cash and cash equivalents	36,193	41,861	16,805	35,193	**45,737**
Assets held for sale	3,471	–	–	–	**2,275**
	215,099	227,362	219,126	248,732	**248,798**
Total assets	309,745	331,121	326,539	363,199	**363,269**
Current liabilities					
Bank overdraft	–	(1,010)	(103)	–	**(758)**
Other interest-bearing loans and borrowings	(471)	(267)	–	(4,506)	**(900)**
Trade and other payables	(141,529)	(149,422)	(154,320)	(143,369)	**(143,216)**
Employee benefits	(1,080)	(1,102)	(1,491)	(2,428)	**(2,506)**
Income tax payable	(11,139)	(10,184)	(10,747)	(9,546)	**(8,615)**
	(154,219)	(161,985)	(166,661)	(159,849)	**(155,995)**
Non-current liabilities					
Other interest-bearing loans and borrowings	(267)	–	–	(30,000)	**(34,392)**
Employee benefits	(19,432)	(16,124)	(9,837)	(12,216)	**(20,253)**
	(19,699)	(16,124)	(9,837)	(42,216)	**(54,645)**
Total liabilities	(173,918)	(178,109)	(176,498)	(202,065)	**(210,640)**
Net assets	135,827	153,012	150,041	161,134	**152,629**

Notice of AGM

Notice is hereby given that the sixty second Annual General Meeting of Headlam Group plc will be held at the group's distribution facility located at Gorsey Lane, Coleshill, Birmingham, B46 1LW on Friday 25 June 2010 at 10.00 a.m. for the following purposes.

As ordinary business

1. To receive, consider and adopt the Annual Report and Accounts, the Directors' Report and the Independent Auditor's Report for the year ended 31 December 2009.

2. To declare a final dividend for the year ended 31 December 2009 of 7.30 pence per ordinary share.

3. To re-elect as a director Graham Waldron who is retiring by rotation in accordance with the company's articles.

4. To re-elect as a director Dick Peters who is retiring by rotation in accordance with the company's articles.

5. To re-appoint KPMG Audit Plc as Independent Auditor of the company from the conclusion of the meeting until the conclusion of the next general meeting at which accounts are laid before the shareholders.

6. To authorise the directors to determine the Independent Auditor's remuneration.

7. To approve the director's Remuneration Report for the year ended 31 December 2009.

As special business

To consider and, if thought fit, pass the following resolutions of which resolution 8 will be proposed as an ordinary resolution and resolutions 9 to 14 will be proposed as special resolutions:-

8. **Authority to allot shares**
   (a) THAT the directors be generally and unconditionally authorised pursuant to section 551 of the Companies Act 2006 (the "Act") to allot shares in the company, and to grant rights to subscribe for or to convert any security into shares in the company, up to an aggregate nominal amount of £1,122,500 for a period expiring (unless previously renewed, varied or revoked by the company in general meeting) at the end of the 2011 AGM (or, if earlier, at the close of business on 30 June 2011), and save that the company may before such expiry make an offer or agreement which would or might require shares to be allotted, or rights to subscribe for or convert any security into shares to be granted, after expiry of this authority and the directors may allot shares and grant rights in pursuance of any such offer or agreement as if this authority had not expired;

   (b) THAT, subject to paragraph (c), all existing authorities given to the directors pursuant to section 80 of the Companies Act 1985 (the "1985 Act") be revoked by this resolution; and

   (c) THAT paragraph (b) shall be without prejudice to the continuing authority of the directors to allot shares (or relevant securities, as that term is defined in the 1985 Act) or grant rights to subscribe for or convert any security into shares (or relevant securities), pursuant to an offer or agreement made by the company before the expiry of the authority pursuant to which such offer or agreement was made.

9. **Dis-application of pre-emption rights**
   THAT, subject to the passing of resolution 8 in this Notice of AGM ("Notice") and in place of all existing powers given to the directors pursuant to section 95 of the 1985 Act, the directors be generally empowered pursuant to section 570 and section 573 of the Act to allot equity securities (as defined in section 560 of the Act) for cash, pursuant to the authority conferred by resolution 11 in this Notice, as if section 561 of the Act did not apply to the allotment. This power:

   (a) expires (unless previously renewed, varied or revoked by the company in general meeting) at the end of the 2011 AGM if passed (or, if earlier, at the close of business on 30 June 2011), save that the company may, before such expiry, make an offer or agreement which would or might require equity securities to be allotted after such expiry and the directors may allot equity securities in pursuance of any such offer or agreement as if this power had not expired; and

Notice of AGM
continued

(b) shall be limited to:

(i) the allotment of equity securities in connection with an issue to holders of ordinary shares of 5 pence in the capital of the company in proportion (as nearly as may be practicable) to their existing holdings and to people who hold other equity securities, if this is required by the rights of those securities or, if the directors consider it necessary, as permitted by the rights of those securities and so that the directors may impose any limits or restrictions and make any arrangements which they consider necessary or appropriate to deal with treasury shares, fractional entitlements, record dates, legal, regulatory or practical problems in, or under the laws of, any territory or any other matter; and

(ii) the allotment of equity securities for cash otherwise than pursuant to paragraph 12(b)(i) up to an aggregate nominal amount of £213,000.

This power applies in relation to a sale of shares which is an allotment of equity securities by virtue of section 560(3) of the Act as if, in the first paragraph of this resolution, the words "pursuant to the authority conferred by resolution 8 in this Notice" were omitted.

10. Authority to purchase own shares

THAT the company be and is hereby generally and unconditionally authorised for the purposes of section 701 of the Act to make market purchases (within the meaning of section 693(4) of the Act) of ordinary shares of 5 pence in the capital of the company, subject to the following conditions:

(a) the maximum number of ordinary shares which may be purchased is 8,536,000;

(b) the minimum price (exclusive of expenses) which may be paid for an ordinary share is 5 pence;

(c) the maximum price (exclusive of expenses) which may be paid for each ordinary share is the higher of: (i) an amount equal to 105% of the average of the middle market quotations of an ordinary share of the company as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the share is contracted to be purchased; and (ii) an amount equal to the higher of the price of the last independent trade of an ordinary share and the highest current independent bid for an ordinary share as derived from the London Stock Exchange Trading System; and

(d) the authority conferred by this resolution shall expire at the conclusion of the 2011 AGM or, if earlier, at the close of business on 30 June 2011 (except in relation to the purchase of shares the contract for which was made before the expiry of this authority and which might be concluded wholly or partly after such expiry).

11. Shareholder rights directive

That the company be and is hereby generally and unconditionally authorised to hold general meetings (other than annual general meetings) on 14 days' clear notice from the date of the passing of this resolution, provided that the authority shall expire at the conclusion of the AGM of the company to be held in 2011 or 30 June 2011, whichever is the earlier.

12. Amendment of Articles

THAT with effect from the conclusion of the AGM:

(a) the Articles of Association of the company be amended by deleting all the provisions of the company's Memorandum of Association ("Memorandum") which, by virtue of section 28 of the Act, are to be treated as provisions of the company's Articles of Association; and

(b) the Articles of Association produced to the AGM, and initialled by the Chairman of the AGM for the purposes of identification, be and hereby are adopted as the Articles of Association of the company (the "New Articles") in substitution for, and to the exclusion of, the existing Articles of Association (the "Current Articles").

Notice of AGM
continued

13. Headlam Group Co-Investment Plan 2008
That the Remuneration committee be and it is hereby authorised to adopt the amendments to the Headlam Group Co-Investment Plan 2008 (the "Co-Investment Plan") shown in the version of the Co-Investment Plan rules which has been produced to the meeting and initialled by the Chairman (for the purposes of identification) and a summary of the main provisions of which amendments is set out in the explanatory notes on page 111 and to do all such acts and things as may be necessary or expedient to give effect to the same.

14. Headlam Group Performance Share Plan 2008
That the Remuneration committee be and it is hereby authorised to adopt the amendments to the Headlam Group Performance Share Plan 2008 (the "Performance Share Plan") shown in the version of the Performance Share Plan rules which has been produced to the meeting and initialled by the Chairman (for the purposes of identification) and a summary of the main provisions of which amendments is set out in the explanatory notes on page 111 and to do all such acts and things as may be necessary or expedient to give effect to the same.

By order of the board

Geoff Duggan
Company Secretary
19 March 2010

Headlam Group plc
Registered No. 460129, England
Registered office:
Gorsey Lane
Coleshill
Birmingham
B46 1LW

Notice of AGM
continued

Explanatory Notes to the Notice of Meeting

Notes 1 to 16 below give further explanation as to the proxy, voting and attendance procedures at the AGM.

1. Entitlement to appoint proxies.

A member entitled to attend and vote at the meeting is also entitled to appoint a proxy or proxies to attend, speak and vote instead of him. A member may appoint more than one proxy in relation to the meeting, provided that each proxy is appointed to exercise the rights attached to a different share or shares held by that member. A proxy need not be a member of the company. Appointment of a proxy will not preclude a member from attending and voting in person at the meeting. To appoint more than one proxy, a member must complete a photocopy of the enclosed proxy card or obtain additional forms from Capita Registrars, tel 0871 6640300 (calls cost 10p per minute plus network charges). Lines are open 8.30am – 5.30pm Monday to Friday. Please also indicate by ticking the relevant box if the proxy appointment is one of multiple appointments being made. Multiple proxy appointments should be returned together in the same envelope. Enter in the box provided the number of shares in relation to which your proxy is authorised or leave the box blank to authorise your proxy to act in relation to your full voting entitlement.

2. Appointing proxies

To be effective, the instrument appointing a proxy and any power of attorney or other authority under which it is executed (or a notarially certified copy of such power or authority) must reach Capita Registrars, Proxies Department, The Registry, 34 Beckenham Road, Beckenham, Kent, BR3 4TU not less than 48 hours before the time for holding the meeting. A form of proxy is enclosed with this Notice.

3. Electronic proxy appointment through Crest

CREST members who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so by using the procedures described in the CREST Manual. CREST personal members or other CREST sponsored members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s) who will be able to take the appropriate action on their behalf.

In order for a proxy appointment or instruction made using the CREST service to be valid, the appropriate CREST message (a "CREST Proxy Instruction") must be properly authenticated in accordance with Euroclear UK & Ireland Limited's ("Euroclear UK & Ireland") specifications and must contain the information required for such instructions, as described in the CREST manual. The message, regardless of whether it constitutes the appointment of a proxy or is an amendment to the instruction given to a previously appointed proxy must, in order to be valid, be transmitted so as to be received by the issuer's agent (ID RA10) by the latest time for the receipt of proxy appointments specified in note 2 above. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by CREST application host) from which the issuer's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.

CREST members and, where applicable, their CREST sponsors, or voting service providers should note that Euroclear UK and Ireland does not make available special procedures in CREST for any particular message. Normal system timing and limitations will, therefore, apply in relation to the input of CREST proxy instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member, or sponsored member, or has appointed a voting service provider, to procure that his CREST sponsor or voting service provider(s) take(s)) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting service providers are referred, in particular, to those sections of the CREST manual concerning practical limitations of the CREST systems and timing.

The company may treat as invalid a CREST proxy instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertified Securities Regulations 2001.

4. Joint holders

In the case of joint holders of a share the vote of the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders. For this purpose seniority is determined by the order in which the names of the holders stand in the register of members in respect of the joint holding.

Notice of AGM
continued

5. Entitlement to attend and vote
Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, the time by which a person must be entered on the register of members in order to have the right to attend and vote at the AGM is 6.00 p.m. on 23 June 2010 or, if the meeting is adjourned, 6.00 p.m. on the date two days before the date for the adjourned meeting. Changes to entries on the register of members after that time will be disregarded in determining the right of any person to attend or vote at the meeting.

6. Nominated person
If you are a person who has been nominated under section 146 of the Companies Act 2006 to enjoy nomination rights (a "Nominated Person") you may, under an agreement between you and the member of the company who has nominated you, have a right to be appointed (or have someone else appointed) as a proxy for the meeting. If you do not have such a proxy appointment right, or you do but do not wish to exercise it, you may have a right to give instructions to the member who has appointed you as to the exercise of voting rights. If you are a Nominated Person, the statement of the rights of members in relation to the appointment of proxies above does not apply. Such rights can only be exercised by registered member of the company.

7. Issued share capital
As at 19 March 2010 the company's issued share capital, including treasury shares, consisted of 85,363,743 ordinary shares of 5p ("shares"). Of these 2,248,647 shares were held in treasury, the voting rights and entitlement to dividend of which were automatically suspended. Accordingly, the total number of voting rights in the company as at that date was 83,115,096.

8. Right to ask questions
A shareholder attending the meeting has the right to ask questions relating to the business being dealt with at the meeting in accordance with section 319A of the Act. In certain circumstances prescribed by section 319A of the Act, the company need not answer a question.

9. Shareholder requests under section 527 of the Act
Under section 527 Companies Act 2006, members of the company representing at least 5% of the total voting rights of the company or at least 100 members who have a right to vote and hold shares in the company on which there has been paid up an average sum per member of at least £100, may require the company to publish on its website a statement setting out any matter relating to the audit of the company's accounts or any circumstances connected with KPMG Audit Plc ceasing to hold office since the last AGM that the members propose to raise at the meeting. Where the company is required to publish such a statement on its website, it may not require the members making the request to pay its expenses in complying with the request. The company must forward the statement to the company's auditor not later than the time when it makes the statement available on its website. The business of the meeting includes any such statement that the company has been required to publish on its website.

10. Non shareholder attendance
Persons who are not shareholders in the company will not be admitted to the meeting unless prior arrangements are made with the company.

11. Access arrangements
Should any shareholder with special needs wish to attend the meeting, please contact the company so that appropriate arrangements can be made.

12. Communicating with the company in relation to the AGM
Except as provided above, members who wish to communicate with the company in relation to the AGM should do so using the following means:
(a) by writing to the Company Secretary at the company's registered office address at Gorsey Lane, Coleshill, Birmingham, B46 1LW; or
(b) by writing to : Capita Registrars, Northern House, Woodsome Park, Fenay Bridge, Huddersfield, HD8 0LA.

No other methods of communication will be accepted. In particular, you may not use any electronic address provided either in this notice or in any related documents (including, without limitation, the Annual Report and Accounts 2009 and the form(s) of proxy) to communicate with the company for any purpose other than those expressly stated in this notice or in such other related documents.

Notice of AGM
continued

13. Inspection of documents
Copies of the directors' service contracts and, where appropriate, letters of appointment, a summary of the directors' transactions in the company's shares during the year and the written terms of reference for each of the Remuneration, Audit and Nomination committees will be available for inspection at the registered office of the company during normal business hours on any weekday (Saturday, Sundays and public holidays excluded) from the date of this Notice until the close of business on the business day preceding the AGM and will also be available for inspection for at least 15 minutes prior to the meeting and throughout the meeting. There are no service agreements between any director and any subsidiary of the company.

In addition, a copy of the current Articles of Association of the company, and the Articles of Association of the company proposed to be adopted by Resolution 12(b) along with the rules of the Plans marked to show the proposed amendments to be adopted by resolutions 13 and 14 will be available for inspection at Pinsent Masons LLP, CityPoint, One Ropemaker Street, London EC2Y 9AH during normal business hours until the conclusion of the meeting and at the place of the meeting on 25 June 2010 for at least 15 minutes prior to the meeting until its conclusion.

14. Voting Results
The results of the voting at the AGM will be announced through a Regulatory Information Service and will appear on our website www.headlam.com.

15. Website
A copy of this Notice, and other information required by section 311A of the Act, can be found at www.headlam.com.

16. Data protection statement
Your personal data includes all data provided by you, or on your behalf, which relates to you as a shareholder, including your name and contact details, the votes you cast and your Reference Number (attributed to you by the company). The company determines the purposes for which and the manner in which your personal data is to be processed. The company and any third party to which it discloses the data (including the company's Registrars) may process your personal data for the purposes of compiling and updating the company's records, fulfilling its legal obligations and processing the shareholder rights you exercise.

Explanatory Notes

EXPLANATORY NOTES

This year's AGM will be held at the group's distribution facility in Coleshill, Birmingham on Friday 25 June 2010 at 10.00 a.m. A description of the resolutions that will be proposed at the meeting is set out below.

Resolutions 1 to 8 (inclusive) are proposed as ordinary resolutions, which means that for each of these resolutions to be passed, more than half the votes cast must be cast in favour of the resolution. Resolutions 9 to 14 (inclusive) are proposed as special resolutions, which means that for each of those resolutions to be passed, at least three quarters of the votes cast must be cast in favour of the resolution.

Resolution 1 – Annual report and accounts
The company is required by law to present to shareholders at the AGM its audited accounts and the directors and independent auditors' reports for the financial year ended 31 December 2009. Shareholders are invited to vote to receive and adopt the Annual Report and Accounts for the year ended 31 December 2009.

Resolution 2 – Declaration of dividend
The directors recommend the payment of a final dividend of 7.30p on each of the ordinary shares entitled thereto, which together with the interim dividend of 3.70p, gives a total dividend of 11.00p for the year ended 31 December 2009. Subject to approval of the declaration of the final dividend at the AGM, the final dividend will be paid on 1 July 2010 to the holders of ordinary shares whose names are recorded on the register of members at the close of business on 4 June 2010.

Resolution 3 – Re-election of Graham Waldron as a director
Graham Waldron is retiring by rotation in accordance with the company's articles and is offering himself for re-election by shareholders. Under the current articles, one-third of the directors are required to retire by rotation each year and, in addition, no director may serve for more than three years without being re-elected by shareholders. Graham was appointed to the board in June 1991 most recently being appointed Chairman in June 2006.

Resolution 4 – Re-election of Dick Peters as a director
Dick Peters is retiring by rotation in accordance with the company's articles and is offering himself for re-election by shareholders. Under the current articles, one-third of the directors are required to retire by rotation each year and, in addition, no director may serve for more than three years without being re-elected by shareholders. Dick was appointed a non-executive director in December 2005. He was formerly senior partner for the East Midlands practice of Deloitte & Touche in Nottingham.

Resolution 5 – Re-appointment of Auditor
The company is required to appoint an auditor at each general meeting at which accounts are laid before the company, to hold office until the end of the next such meeting. This resolution proposes the appointment of an auditor. KPMG has expressed its willingness to continue in office.

Resolution 6 – Agreement of Auditor remuneration
In addition to the company's requirement to appoint an auditor, shareholder authority is sought for the directors to determine the remuneration to be paid to the auditor for the period of appointment.

Resolution 7 – Directors' Remuneration Report
Shareholders are being asked to approve the 2009 director's Remuneration Report, which is set out on pages 36 to 42 of the company's Annual Report and Accounts. Whilst the payment of remuneration to the directors is not dependent on the passing of the resolution, the board will take the vote into account when considering the future development and operation of the company's remuneration policy and practice.

Special Business – Resolutions 8 to 14
Resolution 8 – Authority to allot shares
Shareholders are being asked to pass the necessary resolution to grant to the directors a general authority, for the purpose of section 551 of the Companies Act 2006, to allot relevant securities. On this occasion the proposed general authority is to allot up to an aggregate nominal amount of £1,122,500 representing 22,450,000 ordinary shares (27% of the company's ordinary share capital

(excluding treasury shares) in issue at 19 March 2010 (the latest practical date prior to the publication of this report)). As at 19 March 2010, the company held 2,248,647 treasury shares, which represented approximately 2.71% of the company's issued share capital (excluding treasury shares), which the company can cancel or hold for sale or use to meet the obligations under the company's employee share schemes.

This authority will lapse at the conclusion of the AGM to be held in 2011, or, if earlier, on 30 June 2011. Your directors have no current intention of exercising this authority except in connection with the company's employee share schemes.

Resolution 9 – Dis-application of pre-emption rights
Shareholders are being asked to pass a resolution to empower the directors to allot equity securities, or sell treasury shares, for cash as if section 561 of the Companies Act 2006 (which gives shareholders certain pre-emption rights on the issue of shares or rights to subscribe for or convert securities into shares) did not apply to any such allotment. The authority allows the issue or sale of shares of up to an aggregate nominal amount of £1,122,500 representing 22,450,000 ordinary shares in respect of rights issues and other issues pro-rata to existing entitlements, and also allows issues or sales for cash (other than in relation to a rights issue) limited to shares having an aggregate nominal amount of £213,000 (5% of the company's ordinary share capital in issue at 19 March 2010). The authority will lapse at the conclusion of the AGM to be held in 2011 or, if earlier, on 30 June 2011.

The directors confirm that they have no present intention of exercising this authority.

In accordance with The Pre-Emption Group's Statement of Principles available at www.pre-emptiongroup.org.uk, the directors also confirm their intention that no more than 7.5% of the issued share capital of the company (excluding treasury shares) will be issued for cash on a non-pre-emptive basis during any rolling three-year period.

Resolution 10 – Purchase of own shares
The directors believe that it is in the interests of the company and its members to continue to have the flexibility to purchase its own shares and this resolution seeks authority from members to do so. The directors intend only to exercise this authority where, after considering market conditions prevailing at the time, they believe that the effect of such exercise would be to increase the earnings per share and be in the best interests of shareholders generally. The effect of such purchases would either be to cancel the number of shares in issue or the directors may elect to hold them in treasury pursuant to the Companies (Acquisition of Own Shares) (Treasury Shares) Regulations 2003 (the "Regulations"), which came into force on 1 December 2003. The Regulations enable certain listed companies to hold shares in treasury, as an alternative to cancelling them, following a purchase of own shares by a company in accordance with the Companies Act 2006. Shares held in treasury may subsequently be cancelled, sold for cash or used to satisfy share options and share awards under a company's employee share scheme. Once held in treasury, a company is not entitled to exercise any rights, including the right to attend and vote at meetings in respect of the shares. Further, no dividend or other distribution of the company's assets may be made to the company in respect of the treasury shares.

This resolution renews the authority given at the AGM held on 26 June 2009. The authority is in respect of 10% of the company's issued ordinary share capital as at 19 March 2010 and will lapse at the conclusion of the AGM to be held in 2011 or, if earlier, on 30 June 2011. The resolution specifies the maximum and minimum prices at which the shares may be bought. If the company buys any of its shares under the authority proposed by resolution 10, the board will decide at the time whether to cancel them immediately or hold them in treasury. The purchase of shares will be dependent on market conditions and will also take into account the cash generated in the business and other investment opportunities that may arise over time. During the year the company made no purchases of its own shares.

Details of share options outstanding and treasury share movements including details of own shares acquired by the company are shown respectively in notes 20 and 22 to the financial statements.

Resolution 11 – Shareholder rights directive
This will be proposed as a special resolution to approve the holding of general meetings, other than AGMs, on 14 days' notice. Although the company's articles currently permit this, regulations came into force on 3 August 2009 to implement the Shareholder Rights Directive in the UK. These regulations require a shareholder resolution to be passed to authorise general meetings to be held on 14 days' notice. Without the passing of resolution 11, the minimum notice period under the regulations would be 21 days. If resolution 11 is passed by the shareholders, the regulations as currently drafted would only allow the company to call a general

Explanatory Notes
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meeting on 14 days' notice if it were to make a system of electronic voting available to its shareholders in respect of the meeting in question. The directors consider it to be in the best interest of shareholders to pass resolution 11, which is a repeat of the same resolution passed at last year's AGM, in order to prevent being constrained by the regulations implementing the directive. It will be necessary for a similar resolution to be put to shareholders at each subsequent AGM.

Resolution 12 – Articles
It is proposed that the company adopt the new articles in order to update the current articles, primarily to reflect the implementation of the remaining provisions of the Companies Act 2006 ("the Act") which the company has not incorporated into its current articles, the changes required as a result of the coming into force of the Shareholders' Rights Regulations and the Uncertificated Securities Regulations 2001. It is proposed that the new articles will take effect immediately following the conclusion of the AGM.

Set out below is a summary of the principal differences between the current articles of association of the company (the "Current Articles") and the new articles of association (the "New Articles") proposed to be adopted at the forthcoming AGM. Generally, the opportunity has been taken to bring clearer language into the New Articles, to reflect changes made by the Companies Act 2006, the Companies (Shareholders' Rights) Regulations 2009 (the "Shareholders' Rights Regulations") and to conform the language of the New Articles with that used in the model articles for Public Companies produced by the Department for Business, Innovation and Skills. Other than as set out below, the differences between the Current Articles and New Articles are of a minor or technical nature.

Provisions in the Current Articles which replicate provisions contained in the Companies Act 2006 are in the main amended to bring them into line with the Companies Act 2006.

The article numbers set out below are the numbers under the New Articles.

Article 4 – Change of name
Under the Companies Act 1985, a company could only change its name by special resolution. Under the Companies Act 2006, a company will be able to change its name by other means provided for by its articles. To take advantage of this provision, the New Articles enable the directors to pass a resolution to change the company's name.

Article 9 – Redeemable shares
Under the Companies Act 1985, if a company wished to issue redeemable shares, it had to include in its articles the terms and manner of redemption. The Companies Act 2006 enables directors to determine such matters instead, provided they are so authorised by the articles. The New Articles contain such an authorisation. The company has no plans to issue redeemable shares but if it did so the directors would need shareholders' authority to issue new shares in the usual way.

Articles 13 to 17 – Uncertificated Shares
The Current Articles contain only summary provisions regarding holding shares in an uncertificated form. These New Articles set out detailed provisions giving effect to the Uncertificated Securities Regulation 2001, and expressly deal with the holding of shares in uncertificated form and their transfer by means of the CREST system. These articles also set out arrangements whereby the holders of shares in uncertificated form may change such holdings into certificated form (and vice versa).

Article 18 – Right to share certificate
The provisions in the Current Articles which enable shareholders to request more than one share certificate in respect of different shares of the same class have been removed.

Articles 39 to 45 – Transfer of shares
The New Articles contain specific references to the fact that shares may be transferred in uncertificated form, and also make reference to the fact that shares may be admitted to the Official List of the UKLA.

Article 41 – Refusal to register a transfer of shares
The Companies Act 2006 has introduced a new requirement for companies to provide a transferee with reasons for the refusal where the directors refuse to register a transfer of shares. A company is also now under an obligation to register a transfer as soon as is practicable, rather than within two months as was the case under previous legislation. These requirements are reflected in the New Articles.

Explanatory Notes
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Article 45 – Renunciation deemed to be a transfer
This article gives the board the same powers to refuse to give effect to a renunciation of a renounceable letter of allotment as if it would have in the case of a transfer of shares.

Article 50 – Untraceable shareholders
The article has been updated to specifically state that, upon the sale of shares belonging to untraceable shareholders, the company becomes indebted to the former holder for an amount equal to the net proceeds of sale, but that no interest will accrue and be payable to that former holder.

Article 51 – Disclosure of interests
This article has been updated to refer to the new provisions of the Companies Act 2006 which now govern disclosure of interests in shares. In addition, the article has also been updated to reflect current Listing Rule requirements on the sanctions which can be imposed on any shareholder failing to comply with a notice requiring disclosure of interests in shares. The article has also been extended to deal specifically with the circumstances in which restrictions on shares must be lifted and the provision of dividends and shares issued during any restricted period. Where the relevant shares represent less than 0.25 per cent of the issued shares of the same class, the only sanction which can be imposed is the withdrawal of the right to attend or vote at any general meeting.

Article 52 – Alteration of Share Capital
Previously, if a company wanted to purchase its own shares, consolidate or sub-divide its shares or reduce its share capital or other undistributable reserves, in addition to shareholder authority, specific enabling provisions in its articles authorising it to undertake the relevant action were required. Under the Companies Act 2006, a company only requires shareholder authority to do any of these things and it will no longer be necessary for the articles of a company to contain enabling provisions. Accordingly, the relevant enabling provisions are being removed from the Current Articles.

The remaining articles regarding the alteration of share capital have been amended to make it clear that, where fractional entitlements arise on a consolidation of shares, the directors may sell the shares representing such entitlements on the market or otherwise to such person at such time and at such price as they think fit. This is provided that the net proceeds of the disposal are distributed to the member in question, unless such proceeds are £5 or less, in which case they may be retained by the company.

Articles 53 to 54 – General meetings
These articles have been updated to remove references to extraordinary general meetings, which are now termed 'general meetings' under the Companies Act 2006. Also, to reflect the Companies Act 2006, this article has been amended to allow a general meeting (other than an annual general meeting) to consider a special resolution to be convened on 14 days' notice whereas previously 21 days' notice was required. In accordance with the Shareholder Rights Directive 2009, the company intends to apply annually for shareholder approval to hold general meetings (other than annual general meetings) on 14 days notice.

Article 61 – Security arrangements of general meetings
In line with current market practice, the New Articles contain provisions which allow the board to eject any attendees who cause the proceedings to become disorderly.

Article 60 – Procedure if quorum not present
Under the Companies Act 2006 as amended by the Shareholders' Rights Regulations, general meetings adjourned for lack of quorum must be held at least 10 clear days after the original meeting. The Current Articles have been changed to reflect this requirement.

Article 66 – Amendments to resolutions
The New Articles reflect the common law position that no amendments to special resolutions (other than an amendment to correct an obvious error) may be considered or voted upon. The New Articles further state that an amendment to an ordinary resolution may be considered at a meeting of the company if notice of the amendment has been received by the company at least 48 hours before the meeting or if the chairman decides to accept or propose an amendment of a minor or formal nature or to correct a manifest error or one which he considers fit for consideration. The New Articles also provide that if the chairman consents, an amendment may be withdrawn by its proposer before it is put to the vote.

Explanatory Notes
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Article 67 – Method of voting
To reflect the provisions of the Companies Act 2006, this article specifically includes the right of a single shareholder to demand a poll on a resolution to authorise an off-market purchase of its own shares by the company.

Articles 74 to 79 – Votes of members
Under the Companies Act 2006 proxies are entitled to vote on a show of hands whereas under the Current Articles proxies are only entitled to vote on a poll. Additionally the Shareholders' Rights Regulations have amended the Companies Act 2006 in order to enable proxies appointed by more than one member in which case the proxy has one vote for and one vote against if the proxy has been instructed by one or more members to vote for the resolution and by one or more members to vote against the resolution. The New Articles reflect this new legal position.

Articles 80 to 85 – Appointment of Proxies
The New Articles make it clear that multiple proxies may be appointed in respect of one member's shareholding in the company, provided that each proxy is appointed to exercise the rights attached to a different share or shares held by that member. In addition to the amendments made to allow proxies to vote on a show of hands as well as a poll, the New Articles allow for the appointment of proxies in electronic as well as hard copy form.

Article 85 – Determination of proxy's authority
The New Articles provide that determination of the authority of a proxy or corporate representative is effective only if notice of determination is received by the company at least two hours prior to the time of the meeting (no time period is provided in the Current Articles). The New Articles also extend the ability of a shareholder to determine the authority of an appointed proxy or corporate representative up to two hours prior to the time of any poll taken after the date of the meeting at which it is demanded.

Article 86 – Representatives of corporations
The New Articles entitle the company to appoint multiple corporate representatives, in line with the Companies Act 2006.

Article 87 – Class meetings
The New Articles specifically allow a poll to be called at a class meeting.

Article 89 – Appointment and retirement of directors
Under the Current Articles, one third of the directors are required to retire annually at each AGM, regardless of the length of time served on the board by the director in question. The New Articles provide that, in line with current recommended best practice for listed companies, each director shall retire and be eligible for reappointment at the third AGM after the general meeting at which he was appointed or last reappointed.

Article 96 – Vacation of Director's office
The New Articles allow for the removal of a director from office if he is convicted of a criminal offence (other than a motoring offence or series of offences not resulting in disqualification) and the directors resolve that his office is vacated.

Article 98 – Alternate directors
This article has been extended so that, in addition to the provisions within the Current Articles, the appointment of an alternate director will also be revoked where the individual is not a director and the board revokes its approval of him by resolution.

Article 140 – Notice of Board meetings
Under the Current Articles, it is not necessary to give notice of meetings of directors to any director who is absent from the UK. This provision has been amended, as modern communications mean that there may be no particular obstacle to giving notice to a director who is abroad. It has been replaced with a more general provision that a director is treated as having waived his entitlement to notice, unless he supplies the company with the information necessary to ensure that he receives notice of a meeting before it takes place. The New Articles also provide that notice of directors' meetings may also be served electronically.

Article 167 – Delivery of annual accounts
The Companies Act 2006 enables companies to send to their shareholders a summary of financial statements instead of the present full audited accounts. This article permits the company to take advantage of these provisions but this will not affect the rights of shareholders to receive the full audited accounts should they so wish.

Explanatory Notes
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Articles 170 to 177 – Notices
The Companies Act 2006 enables companies to communicate with members by electronic and/or website communications. The New Articles allow communications to members in electronic form and, in addition, they also permit the company to take advantage of the provisions relating to website communications. Before the company can communicate with a member by means of website communication, under the Companies Act 2006, the relevant member must be asked individually by the company to agree that the company can send or supply documents or information to him by means of a website. Further, the company must either have received a positive response or have received no response within the period of 28 days beginning with the date on which the request was sent. The company will notify the member (either in writing, or by other permitted means) when a relevant document or information is placed on the website and a member can always request a hard copy version of the document or information. The company has no current intention of seeking individual shareholder consent to allow communications with shareholders by means of a website, however the board considers it prudent to include the relevant authorities within the New Articles which would be required to allow such communication, should the board decide to use website communication in the future.

Article 175 – Untraced member not entitled to notices
This article allows the company to stop sending notices to a shareholder if the despatch of cheques or warrants to that shareholder has been suspended in accordance with the New Articles or if two consecutive notices to the shareholder's registered address or address for service have been returned undelivered. The company will resume sending notices if the shareholder supplies a new registered address or address for service.

In addition to the above, the following provisions of the Current Articles have no equivalent in the New Articles:-

General – Extraordinary Resolutions
The Current Articles contain provisions which refer to extraordinary resolutions. These provisions have been amended or removed as appropriate, as the concept of extraordinary resolutions has not been retained under the Companies Act 2006.

Article 5 of the Current Articles – Authorised share capital
This provision of the Current Articles has been amended to reflect the abolition under the Companies Act 2006 of the concept of authorised share capital as from 1 October 2009. Directors will still be limited as to the number of shares they can at any time allot because allotment authority continues to be required under the Companies Act 2006, save in respect of Employee share schemes.

Article 12 of the Current Articles – Purchase of own shares
Previously, if a company wanted to purchase its own shares, consolidate or sub-divide its shares or reduce its share capital or other undistributable reserves, in addition to shareholder authority, it required specific provisions in its Articles authorising it to undertake the relevant action. Under the Companies Act 2006 , a company will require only shareholder authority to do any of these things and it will no longer be necessary for the Articles to contain enabling provisions. Accordingly, the relevant enabling provisions are being removed from the New Articles.

Article 47 – Suspension of registration of share transfers
The Current Articles permit the directors to suspend the registration of transfers. Under the Companies Act 2006 share transfers must be registered as soon as practicable. The power in the Current Articles to suspend the registration of transfers is inconsistent with this requirement. Accordingly, this power has been removed in the New Articles.

THE COMPANY'S OBJECTS

The provisions regulating the operations of the company are currently set out in the company's Memorandum and Articles of Association. The company's Memorandum contains, among other things, the objects clause which sets out the scope of the activities the company is authorised to undertake. This is drafted to give a wide scope.

The Companies Act 2006 significantly reduces the constitutional significance of a company's memorandum. The Companies Act 2006 provides that a memorandum will record only the names of subscribers and the number of shares each subscriber has agreed to take in the company. Under the Companies Act 2006 the objects clause and all other provisions which are contained in a company's memorandum, for existing companies at 1 October 2009, are deemed to be contained in the company's articles of association but the company can remove these provisions by special resolution. Further, the Companies Act 2006 states that unless a company's articles provide otherwise, a company's objects are unrestricted. This abolishes the need for companies to have objects clauses.

Explanatory Notes
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For this reason the company is proposing to remove its objects clause together with all other provisions of its memorandum which, by virtue of the Companies Act 2006, are treated as forming part of the company's Articles of Association as of 1 October 2009. Resolution 12 confirms the removal of these provisions for the company. As the effect of this resolution will be to remove the statement currently in the company's Memorandum of Association regarding limited liability, the New Articles also contain an express statement regarding the limited liability of shareholders.

Resolutions 13 and 14 – Headlam Group Co-Investment Plan 2008 and the Headlam Group Performance Share Plan 2008
The Headlam Group Co-Investment Plan 2008 (the "Co-Investment Plan") and the Headlam Group Performance Share Plan 2008 (the "Performance Share Plan" and together with the Co-Investment Plan, the "Plans") were approved by the company's shareholders at the AGM on 20 June 2008. No awards under the Plans have yet been made.

Under the Co-Investment Plan, participants may be invited to take up to 100 per cent. of their annual bonus in the form of ordinary shares in the company ("Shares"). The net (after tax and national insurance contributions ("NICs")) amount of the gross figure so specified is used to acquire Shares ("Bonus Award Shares"). Subject to the discretion of the Remuneration committee of the board of directors of the company (the "Committee") to determine higher or lower amounts for any financial year ("Year"), an eligible employee who wishes to participate will be required to apply not less than 15 per cent of his bonus for the relevant Year in the acquisition of Bonus Award Shares. If no annual bonus is paid in a Year, the Committee may permit investment of other funds, but subject to a maximum of 50 per cent of any bonus paid in the preceding Year.

As adopted, the Co-Investment Plan provided that for any awards made relating to the Year ended 31 December 2007, the Committee could determine that a participant in addition to, or in substitution for, the purchase of Shares out of his net bonus for the Year ended 31 December 2007, could deposit for the purposes of the Co-Investment Plan share certificates or other evidence of title to Shares which he purchased, already held or which were held under arrangements agreed with the Committee ("Nominated Shares"). Nominated Shares were to be subject to a limit of such number of Shares, the market value of which, as at the date of nomination, was equal to not less than 15 per cent and not more than 100 per cent of the bonus paid to the participant for the Year ended 31 December 2007. Nominated Shares were to be treated for all purposes of the Co-Investment Plan as Bonus Award Shares.

A matching Share award ("Matching Share Award") may be made to a participant in the Co-Investment Plan, in the form of a nil-cost option to acquire shares. Matching Share Awards will be subject to performance targets. If, generally, Bonus Award Shares are retained by a participant throughout the performance period (or the participant's interest in the Bonus Award Shares is so retained); the participant remains employed within the group throughout the performance period and the performance target for the Matching Share Award is met, the participant will acquire additional shares ("Matching Shares") under the Matching Share Award. The number of Matching Shares which may be so acquired will be in direct proportion to the number of Bonus Award Shares acquired or deposited in relation to the relevant award. There is a maximum level of matching ratio, of twice the number of Shares that could have been acquired with the pre-tax amount of bonus (or other funds) by reference to which the associated Bonus Award Shares were purchased (or, in the case of any awards made relating to the Year ended 31 December 2007, twice the value of the Nominated Shares, grossed up for income tax and employees' NICs).

The Co-Investment Plan was not operated in respect of the Year ended 31 December 2007, such that the provisions relating to "Nominated Shares" were not applied. Accordingly, it is proposed that the rules of the Co-Investment Plan be amended to provide that Shares may be deposited as "Nominated Shares" for the purposes of a participant's first award under the Co-Investment Plan (a "First Award") up to a maximum value of the participant's annual basic salary prevailing at the date at which the First Award is made, the effect of which will be to enable a participating employee to deposit for the purposes of his First Award share certificates or other evidence of title to Shares which he purchases, already holds or which are held under such arrangements as are agreed with the Committee, up to the specified limit and to be granted a Matching Share Award in respect of such number of Nominated Shares, with the level of match being up to two times the value of the Nominated Shares, grossed up for income tax and employees' NICs.

It is considered appropriate to amend the Co-Investment Plan in this way in order that it can be operated in a similar manner to that which was originally envisaged and so that flexibility in relation to how it can operate is retained and to extend the ability to deposit Nominated Shares to all eligible employees in respect of their First Award because this aspect of the Co-Investment Plan will no longer be time limited.

Explanatory Notes
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Awards under the Co-Investment Plan to acquire Matching Shares and awards under the Performance Share Plan can ordinarily be exercised in the period of 90 days following their vesting. Vesting is subject to the satisfaction of a performance condition measured over a period of three years. In order to give participants in the Plans more flexibility as to when they may exercise awards and take benefits, it is proposed that the rules of the Plans be amended to provide that awards can be exercised up to the tenth anniversary of the date of the award, which will give participants a longer period within which they can exercise awards. It is also proposed that the rules of each of the Plans be amended to permit the grant of awards within the period of 42 days following the 2010 AGM, in order that awards can be made on the basis of the amended rules.

The opportunity is also being taken to make certain other minor amendments to the rules of the Plan.

The rules of the Plans marked to show the proposed amendments will be available for inspection at the registered office of the company and also at the offices of Pinsent Masons LLP, CityPoint, One Ropemaker Street, London, EC2Y 9AH from the date of this Notice until the close of business on the business day preceding the AGM and will also be available for inspection at the place of the AGM for at least 15 minutes prior to the meeting and throughout the meeting.

Shareholder Information

Shareholder helpline
Headlam's shareholder register is maintained by Capita Registrars ("Capita"), who are responsible for making dividend payments and updating the register, including details of changes to shareholders' addresses and purchases or sales of Headlam shares. If you have a question about your shareholding in Headlam you should contact: Capita Registrars, Northern House, Woodsome Park, Fenay Bridge, Huddersfield, HD8 0LA. email: ssd@capitaregistrars.com, telephone +44 (0)871 664 0300 (calls cost 10p plus network extras). Lines are open 8.30am – 5.30pm Monday to Friday.

Frequent shareholder enquiries
If you change your address
Please notify Capita in writing. If shares are held in joint names, the notification must be signed by all named shareholders.

If you change your name
Please notify Capita in writing and enclose a copy of any marriage certificate or change of name deed as evidence.

Lost Headlam share certificate
If your share certificate is lost or stolen, you should call Capita immediately. A letter of indemnity will be sent to you to sign. Capita will charge for this service.

Duplicate shareholder accounts
If you receive more than one copy of Headlam communications you may have your shares registered inadvertently in at least two accounts. This happens when the registration details of separate transactions differ slightly. If you wish to consolidate such multiple accounts, call Capita to request the accounts are consolidated.

Buying and selling shares in the UK
If you wish to trade in Headlam shares, you can do so at Capita's website, www.capitadeal.com or alternatively use a stockbroker or high street bank which trades on the London Stock Exchange. There are many telephone and online services available. If you are selling, you will need to present your share certificate at the time of sale.

Transferring Headlam shares
Transferring shares to someone else requires the completion of a stock transfer form. This form, and details of the procedure you need to follow, is available from Capita's website. Stamp duty is not normally payable if the transfer is to a relative or if there is no money being paid in exchange for the shares.

Share prices information
Shareholders can find share prices listed in most national newspapers. Ceefax and Teletext pages also display share prices that are updated regularly throughout the trading day. For a real-time buying or selling price, you should contact a stockbroker. Additionally there is a link to the London Stock Exchange on the Headlam website.

The Headlam website
The Headlam website at www.headlam.com provides news and details of the company's activities, plus information on the share price. The investor information section of the website contains up-to-date information for shareholders including the company's latest results and key dates such as dividend payment dates.

ShareGift
ShareGift, the charity share donation scheme, is a free service for shareholders wishing to give shares to charitable causes. It may be especially useful for those who wish to dispose of a small parcel of shares which would cost more to sell than they are worth. There are no capital gains tax implications (i.e. no gain or loss) on gifts of shares to charity and it is also possible to obtain income tax relief. Further information can be obtained at www.sharegift.org

The Unclaimed Assets Register
The Unclaimed Assets Register is a unique search service that helps individuals to find their lost assets and re-establish contact with financial institutions. It has a database of unclaimed life policies, pensions, unit trust holdings, and share dividends drawn from many companies and can search for lost assets and entitlements. The Unclaimed Assets Register charges a small fixed fee for each search, 10% of which goes to charity. For further information, visit www.uar.co.uk

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