

MOHAWK INDUSTRIES INC
Form 10-Q
November 07, 2007

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

FORM 10 Q

[Mark One]

**[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 29, 2007

OR

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

For the transition period from to

**Commission File Number
01 19826**

**MOHAWK INDUSTRIES, INC.
(Exact name of registrant as specified in its charter)**

**Delaware
(State or other jurisdiction of incorporation or organization)**

**52 1604305
(I.R.S. Employer Identification No.)**

**P. O. Box 12069, 160 S. Industrial Blvd., Calhoun, Georgia
(Address of principal executive offices)**

**30701
(Zip Code)**

Registrant's telephone number, including area code: (706) 629 7721

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act):

Large accelerated filer [x] Accelerated filer [] Non-accelerated filer []

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

The number of shares outstanding of the issuer's classes of common stock as of November 5, 2007, the latest practicable date, is as follows: 79,386,149 shares of Common Stock, \$.01 par value.

MOHAWK INDUSTRIES, INC.

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PART I. FINANCIAL INFORMATION

ITEM I. FINANCIAL STATEMENTS

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

(In thousands)

(Unaudited)

| | September 29, 2007 | December 31, 2006 |
|--|--------------------|-------------------|
| Current assets: | | |
| Cash and cash equivalents | \$ 81,664 | 63,492 |
| Receivables | 958,947 | 876,206 |
| Inventories | 1,297,605 | 1,225,874 |
| Prepaid expenses | 111,494 | 114,088 |
| Deferred income taxes | 157,665 | 99,251 |
| Total current assets | 2,607,375 | 2,378,911 |
| Property, plant and equipment, at cost | 3,222,328 | 3,068,522 |
| Less accumulated depreciation and amortization | 1,285,730 | 1,180,434 |
| Net property, plant and equipment | 1,936,598 | 1,888,088 |

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| | | |
|-------------------------|--------------|-----------|
| Goodwill | 2,784,760 | 2,699,639 |
| Tradenames | 693,570 | 662,314 |
| Other intangible assets | 477,895 | 517,780 |
| Other assets | 26,972 | 31,662 |
| | \$ 8,527,170 | 8,178,394 |

See accompanying notes to condensed consolidated financial statements.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY
(In thousands, except per share data)

(Unaudited)

September 29, 2007 December 31, 2006

Current liabilities:

| | | |
|---------------------------------------|------------|-----------|
| Current portion of long-term debt | \$ 337,351 | 576,134 |
| Accounts payable and accrued expenses | 1,022,114 | 1,019,629 |
| Total current liabilities | 1,359,465 | 1,595,763 |
| Deferred income taxes | 641,163 | 628,311 |
| Long-term debt, less current portion | 2,126,936 | 2,207,547 |
| Other long-term liabilities | 151,874 | 31,510 |
| Total liabilities | 4,279,438 | 4,463,131 |

Stockholders' equity:

| | | |
|--|-----|-----|
| Preferred stock, \$.01 par value; 60 shares authorized; no shares issued | - | - |
| Common stock, \$.01 par value; 150,000 shares authorized; 79,349 and 78,816 shares issued in 2007 and 2006, respectively | 793 | 788 |

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| | | |
|---|---------------------|------------------|
| Additional paid-in capital | 1,198,177 | 1,152,420 |
| Retained earnings | 3,083,230 | 2,755,529 |
| Accumulated other comprehensive income, net | 289,250 | 130,372 |
| | 4,571,450 | 4,039,109 |
| Less treasury stock at cost; 11,046 and 11,051 shares in 2007 and 2006, respectively | 323,718 | 323,846 |
| Total stockholders' equity | 4,247,732 | 3,715,263 |
| | \$ 8,527,170 | 8,178,394 |

See accompanying notes to condensed consolidated financial statements

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except per share data)
(Unaudited)

| | Three Months Ended September 29, 2007 | September 30, 2006 |
|---|--|--------------------|
| Net sales | \$ 1,937,677 | 2,024,019 |
| Cost of sales | 1,392,294 | 1,455,508 |
| Gross profit | 545,383 | 568,511 |
| Selling, general and administrative expenses | 344,569 | 345,771 |
| Operating income | 200,814 | 222,740 |
| Other expense (income): | | |
| Interest expense | 37,518 | 44,655 |
| Other expense | 8,541 | 2,668 |
| Other income | (9,340) | (2,613) |
| U.S. Customs refund, net | - | (8,834) |
| | 36,719 | 35,876 |
| Earnings before income taxes | 164,095 | 186,864 |
| Income taxes | 42,041 | 59,156 |
| Net earnings | \$ 122,054 | 127,708 |
| Basic earnings per share | \$ 1.79 | 1.89 |
| Weighted-average common shares outstanding | 68,281 | 67,704 |
| Diluted earnings per share | \$ 1.78 | 1.88 |
| Weighted-average common and dilutive potential common shares outstanding | 68,597 | 68,021 |

See accompanying notes to condensed consolidated financial statements.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except per share data)
(Unaudited)

| | Nine Months Ended September 29, 2007 | September 30, 2006 |
|---|---|--------------------|
| Net sales | \$ 5,778,750 | 6,007,248 |
| Cost of sales | 4,153,229 | 4,330,015 |
| Gross profit | 1,625,521 | 1,677,233 |
| Selling, general and administrative expenses | 1,055,882 | 1,067,547 |
| Operating income | 569,639 | 609,686 |
| Other expense (income): | | |
| Interest expense | 118,235 | 131,113 |
| Other expense | 17,394 | 9,777 |
| Other income | (16,717) | (3,397) |
| U.S. Customs refund, net | (9,154) | (15,066) |
| | 109,758 | 122,427 |
| Earnings before income taxes | 459,881 | 487,259 |
| Income taxes | 132,181 | 160,917 |
| Net earnings | \$ 327,700 | 326,342 |
| Basic earnings per share | \$ 4.81 | 4.82 |
| Weighted-average common shares outstanding | 68,118 | 67,654 |
| Diluted earnings per share | \$ 4.79 | 4.80 |
| Weighted-average common and dilutive potential common shares outstanding | 68,461 | 68,056 |

See accompanying notes to condensed consolidated financial statements.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

| | Nine Months Ended September 29, 2007 | September 30, 2006 |
|--|---|--------------------|
| Cash flows from operating activities: | | |
| Net earnings | \$ 327,700 | 326,342 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Depreciation and amortization | 224,864 | 202,674 |
| Deferred income taxes | 19,470 | (64,026) |
| Loss on disposal and impairment of property, plant and equipment | 8,739 | 5,895 |
| Excess tax benefit from stock-based compensation | (6,336) | (3,022) |
| Stock based compensation expense | 10,635 | 9,028 |
| Changes in operating assets and liabilities, net of effects of acquisition: | | |
| Receivables | (49,729) | (71,280) |
| Inventories | (3,626) | (48,006) |
| Accounts payable and accrued expenses | 54,421 | 165,244 |
| Other assets and prepaid expenses | 20,729 | 18,642 |
| Other liabilities | (5,030) | 4,750 |
| Net cash provided by operating activities | 601,837 | 546,241 |
| Cash flows from investing activities: | | |
| Additions to property, plant and equipment, net | (97,832) | (124,048) |
| Acquisitions, net of cash acquired | (142,772) | (70,907) |
| Net cash used in investing activities | (240,604) | (194,955) |
| Cash flows from financing activities: | | |
| Payments on revolving line of credit | (1,338,613) | (1,290,746) |
| Proceeds from revolving line of credit | 1,214,799 | 1,053,298 |
| Repayment on bridge loan | - | (1,400,000) |
| Proceeds from issuance of senior notes | - | 1,386,841 |
| Net change in asset securitization borrowings | 80,000 | 110,000 |
| Payments on senior notes and term loan | (300,000) | (239,220) |
| Payments of other debt | (248) | (31,904) |
| Excess tax benefit from stock-based compensation | 6,336 | 3,022 |
| Change in outstanding checks in excess of cash | (34,964) | (15,506) |
| Acquisition of treasury stock | - | (5,180) |
| Proceeds from stock option exercises | 28,544 | 9,505 |
| Net cash used in financing activities | (344,146) | (419,890) |

| | | |
|--|-----------|----------|
| Effect of exchange rate changes on cash and cash equivalents | 1,085 | 3,749 |
| Net change in cash | 18,172 | (64,855) |
| Cash, beginning of period | 63,492 | 134,585 |
| Cash, end of period | \$ 81,664 | 69,730 |

See accompanying notes to condensed consolidated financial statements.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

1. Interim reporting

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with instructions to Form 10-Q and do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. These statements should be read in conjunction with the consolidated financial statements and notes thereto, and the Company's description of critical accounting policies, included in the Company's 2006 Annual Report on Form 10-K, as filed with the Securities and Exchange Commission.

2. New Pronouncements

In July 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48 ("FIN 48"), *"Accounting for Uncertainty in Income Taxes-an Interpretation of FASB Statement No. 109,"* which clarifies the accounting for uncertainty in income taxes. FIN 48 prescribes a recognition threshold and measurement criteria for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The Company adopted the provisions of FIN 48 on January 1, 2007. Upon adoption, the Company recognized no change to opening retained earnings.

In September 2006, FASB issued Statement of Financial Accounting Standards ("SFAS") No. 157 ("SFAS No. 157"), *"Fair Value Measurements."* SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of financial instruments according to a fair value hierarchy. Additionally, companies are

required to provide certain disclosures regarding instruments within the hierarchy, including a reconciliation of the beginning and ending balances for each major category of assets and liabilities. SFAS No. 157 is effective for the Company's fiscal year beginning January 1, 2008. The Company is currently evaluating the impact of SFAS No. 157 on its consolidated financial statements.

In September 2006, FASB issued SFAS No. 158 ("SFAS No. 158"), "*Employers' Accounting for Defined Benefit Pension and Other Post Retirement Plans- an amendment of FASB Statements No. 87, 88, 106 and 132(R.)*" The Company adopted all provisions of SFAS No. 158 as of December 31, 2006, except for the measurement date provisions, which are effective for fiscal years ending after December 15, 2008. The Company is currently evaluating the impact of the measurement date provisions of SFAS No. 158 on its consolidated financial statements.

In February 2007, FASB issued SFAS No. 159 ("SFAS No. 159"), "*The Fair Value Option for Financial Assets and Financial Liabilities-including an amendment of FASB Statement No. 115.*" SFAS No. 159 expands the use of fair value accounting but does not affect existing standards which require assets or liabilities to be carried at fair value. The objective of SFAS No. 159 is to improve financial reporting by providing companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. Under SFAS No. 159, a company may elect to use fair value to measure eligible items at a specified election date and report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Eligible items include, but are not limited to, accounts and loans receivable, available-for-sale and held-to-maturity securities, equity method investments, accounts payable, guarantees, issued debt and firm commitments. If elected, SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing whether fair value accounting is appropriate for any eligible items and has not estimated the impact, if any, on its consolidated financial statements.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

3. Receivables

Receivables are as follows:

| | September 29, 2007 | December 31, 2006 |
|--|--------------------|-------------------|
| Customers, trade | \$ 1,020,175 | 932,022 |
| Other | 37,701 | 47,798 |
| | 1,057,876 | 979,820 |
| Less allowance for discounts, returns, claims and doubtful accounts | 98,929 | 103,614 |
| Net receivables | \$ 958,947 | 876,206 |

4. Inventories

The components of inventories are as follows:

| | September 29, 2007 | December 31, 2006 |
|--------------------------|---------------------|-------------------|
| Finished goods | \$ 823,221 | 806,463 |
| Work in process | 109,430 | 95,746 |
| Raw materials | 364,954 | 323,665 |
| Total inventories | \$ 1,297,605 | 1,225,874 |

5. Intangible assets and goodwill

The components of intangible assets are as follows:

Goodwill:

| | Mohawk | Dal-Tile | Unilin | Total |
|--|--------|----------|--------|-------|
| | | | | |

| | | | | |
|---|------------|-----------|-----------|-----------|
| Balance as of January 1, 2007 | \$ 199,132 | 1,182,790 | 1,317,717 | 2,699,639 |
| Goodwill recognized during the period (1) | - | (700) | 6,071 | 5,371 |
| Effect of translation during the period | - | - | 79,750 | 79,750 |
| Balance as of September 29, 2007 | \$ 199,132 | 1,182,090 | 1,403,538 | 2,784,760 |

(1) The Company reversed certain pre-acquisition tax liabilities in the Dal-Tile and Unilin segments. The Unilin segment also includes the addition of \$12,968 for the acquisition of certain wood flooring assets during the third quarter of 2007. For more information see Note 16.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

| Intangible assets: | Mohawk | Dal-Tile | Unilin | Total |
|---|--------------------|---------------|-------------------|---------------|
| Indefinite life assets not subject to amortization: | | | | |
| Balance as of January 1, 2007, net | \$ 125,580 | 146,700 | 390,034 | 662,314 |
| Effect of translation during period | - | - | 31,256 | 31,256 |
| Balance as of September 29, 2007 | \$ 125,580 | 146,700 | 421,290 | 693,570 |
| Intangible assets subject to amortization: | | | | |
| Balance as of January 1, 2007, net | \$ 42,072 | 1,004 | 474,704 | 517,780 |
| Amortization during period | (2,650) | (516) | (66,603) | (69,769) |
| Effect of translation during period | - | - | 29,884 | 29,884 |
| Balance as of September 29, 2007 | \$ 39,422 | 488 | 437,985 | 477,895 |
| Amortization expense: | Three Months Ended | | Nine Months Ended | |
| | September 29, | September 30, | September 29, | September 30, |
| | 2007 | 2006 | 2007 | 2006 |
| Amortization expense | \$ 23,700 | 20,472 | 69,769 | 60,285 |

6. Accounts payable and accrued expenses

Accounts payable and accrued expenses are as follows:

| | September 29, 2007 | December 31, 2006 |
|--------------------------------------|--------------------|-------------------|
| Outstanding checks in excess of cash | \$ 33,175 | 68,139 |
| Accounts payable, trade | 465,750 | 371,538 |
| Accrued expenses | 285,825 | 297,511 |
| Income taxes payable | 49,779 | 125,046 |

| | | |
|--|---------------------|------------------|
| Deferred tax liability | 5,386 | 4,565 |
| Accrued compensation | 182,199 | 152,830 |
| Total accounts payable and accrued expenses | \$ 1,022,114 | 1,019,629 |

7. Product Warranties

The Company warrants certain qualitative attributes of its products for up to 33 years. The Company records a provision for estimated warranty and related costs, based on historical experience and periodically adjusts these provisions to reflect actual experience. The warranty obligation is as follows:

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

| | Three Months Ended September 29 | | Nine Months Ended September 29, September 30, | |
|--------------------------------|------------------------------------|----------|--|----------|
| | 2007 | 30, 2006 | 2007 | 2006 |
| Balance at beginning of period | \$ 29,920 | 24,824 | 30,712 | 25,988 |
| Warranty claims paid | (13,297) | (11,676) | (41,680) | (36,481) |
| Warranty expense | 16,661 | 12,418 | 44,252 | 36,059 |
| Balance at end of period | \$ 33,284 | 25,566 | 33,284 | 25,566 |

8. Comprehensive income

Comprehensive income is as follows:

| | Three Months Ended September 29 | | Nine Months Ended September 29, September 30, | |
|---|------------------------------------|----------|--|---------|
| | 2007 | 2006 | 2007 | 2006 |
| Net earnings | \$ 122,054 | 127,708 | 327,700 | 326,342 |
| Other comprehensive income: | | | | |
| Foreign currency translation | 109,702 | (16,619) | 157,765 | 132,044 |
| Unrealized (loss) gain on derivative instruments, net of income taxes | 462 | (388) | 1,113 | (2,893) |
| Comprehensive income | \$ 232,218 | 110,701 | 486,578 | 455,493 |

9. Stock compensation

The Company accounts for its stock-based compensation plans in accordance with SFAS No. 123R ("SFAS No. 123R"), *"Share-Based Payment."* Under SFAS No. 123R, all stock based compensation cost is measured at the grant date, based on the estimated fair value of the award, and is recognized as an expense in the statement of earnings over the requisite service period.

Under the Company's 2002 Long-Term Incentive Plan ("2002 Plan"), the Company's principal stock compensation plan prior to May 16, 2007, the Company reserved up to a maximum of 3,200 shares of common stock for issuance upon the grant or exercise of stock options, restricted stock, restricted stock units ("RSU's") and other types of awards, as defined under the 2002 Plan, to directors and key employees through 2012. Option awards, restricted stock and RSU's are generally granted with an exercise price equal to the market price of the Company's common stock on the date of the grant. These awards generally vest between three and five years and have a 10-year contractual term. On May 16, 2007, the Company's stockholders approved the 2007 Long-Term Incentive Plan ("2007 Plan"), under which the Company reserved up to a maximum of 3,200 shares of common stock for issuance upon the grant or exercise of awards under the 2007 Plan. As of September 29, 2007, there have been no awards issued under the 2007 Plan.

The Company recognized stock based compensation costs related to stock options of \$2,158 (\$1,367 net of taxes) and \$6,802 (\$4,309 net of taxes) which has been allocated to selling, general and administrative expenses for the three and nine months ended September 29, 2007, respectively. The Company recognized stock based compensation costs of \$2,919 (\$1,855 net of taxes) and \$9,028 (\$5,701 net of taxes) which has been allocated to selling, general and administrative expenses, for the three and nine months ended September 30, 2006, respectively. Pre-tax unrecognized compensation expense for stock options granted to employees and

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

outside directors, net of estimated forfeitures, was \$13,791 as of September 29, 2007, and will be recognized as expense over a weighted-average period of approximately 2.0 years. Restricted stock awards granted and the related compensation expense was not significant for the three and nine months ended September 29, 2007 and September 30, 2006.

The fair value of the option award is estimated on the date of grant using the Black-Scholes-Merton valuation model. Expected volatility is based on the historical volatility of the Company's common stock. The Company uses historical data to estimate option exercise and forfeiture rates within the valuation model.

The Company recognized stock based compensation costs related to the issuance of RSU's of \$820 (\$519 net of taxes) and \$3,608 (\$2,286 net of taxes) for the three and nine months ended September 29, 2007, respectively, which has been allocated to selling, general and administrative expenses. Pre-tax unrecognized compensation expense for unvested RSU's granted to employees, net of estimated forfeitures, was \$8,325 as of September 29, 2007, and will be recognized as expense over a weighted-average period of approximately 3.1 years.

10. Earnings per share

The Company applies the provisions of SFAS No. 128 ("SFAS No. 128"), "*Earnings per Share*," which requires companies to present basic EPS and diluted EPS. Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company.

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Dilutive common stock options and RSU's are included in the diluted EPS calculation using the treasury stock method. Excluded from the computation of diluted earnings per share are stock options and RSU's of 673 and 1,547 shares because their effect would have been anti-dilutive for the three month period ended September 29, 2007 and 2006, respectively, and 726 shares and 1,316 shares for the nine month period ended September 29, 2007 and 2006, respectively.

| | Three Months Ended | | Nine Months Ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 29, 2007 | September 30, 2006 | September 29, 2007 | September 30, 2006 |
| Net earnings | \$122,054 | 127,708 | 327,700 | 326,342 |
| Weighted-average common and dilutive potential common shares outstanding: | | | | |
| Weighted-average common shares outstanding | 68,281 | 67,704 | 68,118 | 67,654 |
| Add weighted-average dilutive potential common shares - options and RSU's to purchase common shares, net | 316 | 317 | 343 | 402 |
| Weighted-average common and dilutive potential common shares outstanding | 68,597 | 68,021 | 68,461 | 68,056 |
| Basic earnings per share | \$1.79 | 1.89 | 4.81 | 4.82 |
| Diluted earnings per share | \$1.78 | 1.88 | 4.79 | 4.80 |

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

11. Supplemental Condensed Consolidated Statements of Cash Flows Information

| | Nine Months Ended September 29, 2007 | September 30, 2006 |
|--------------------------------------|---|--------------------|
| Net cash paid during the period for: | | |
| Interest | \$ 134,873 | 121,097 |
| Income taxes | \$ 155,036 | 166,108 |

12. Segment reporting

The Company has three reporting segments, the Mohawk segment, the Dal-Tile segment and the Unilin segment. The Mohawk segment manufactures, markets and distributes its product lines, which include carpet, rugs, pad, ceramic tile, hardwood, resilient and laminate, through its network of approximately 50 regional distribution centers and satellite warehouses using company-operated trucks, common carrier or rail transportation. The segment product lines are sold through various selling channels, which include floor covering retailers, home centers, mass merchandisers, department stores, independent distributors, commercial dealers and commercial end users. The Dal-Tile segment manufactures, markets and distributes its product lines, which include ceramic tile, porcelain tile and stone products, through its network of regional distribution centers and approximately 265 company-operated sales service centers using company-operated trucks, common carriers or rail transportation. The segment product lines are purchased by floor covering retailers, home centers, independent distributors, tile specialty dealers, tile

contractors, and commercial end users. The Unilin segment manufactures, markets and distributes its product lines, which include laminate flooring, wood flooring, insulated roofing and other wood-based panels through various selling channels, which include independent retailers, home centers, independent distributors, contractors, and commercial users.

The accounting policies for each operating segment are consistent with the Company's policies for the consolidated financial statements. Amounts disclosed for each segment are prior to any elimination or consolidation entries. Corporate general and administrative expenses attributable to each segment are estimated and allocated accordingly. Segment performance is evaluated based on operating income.

During the third quarter of 2007, the Company recorded a charge of approximately \$8,500 in the Mohawk segment and \$5,700 in the Dal-Tile segment related to plant shutdowns. The charge is reflected within cost of goods sold on the condensed consolidated statements of earnings.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

| Segment information is as follows: | Three Months Ended | | Nine Months Ended | |
|------------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 29, 2007 | September 30, 2006 | September 29, 2007 | September 30, 2006 |
| Net sales: | | | | |
| Mohawk | \$ 1,076,745 | 1,233,833 | 3,237,818 | 3,626,371 |
| Dal-Tile | 497,420 | 501,241 | 1,469,568 | 1,482,065 |
| Unilin | 378,446 | 292,924 | 1,094,073 | 909,319 |
| Intersegment Sales | (14,934) | (3,979) | (22,709) | (10,507) |
| | \$ 1,937,677 | 2,024,019 | 5,778,750 | 6,007,248 |
| Operating income: | | | | |
| Mohawk | \$ 77,002 | 110,505 | 185,177 | 275,111 |
| Dal-Tile | 63,109 | 69,642 | 196,857 | 213,286 |
| Unilin | 71,034 | 49,748 | 213,270 | 149,424 |
| Corporate and Eliminations | (10,331) | (7,155) | (25,665) | (28,135) |
| | \$ 200,814 | 222,740 | 569,639 | 609,686 |
| Assets: | | | | |
| Mohawk | | | \$ 2,391,392 | 2,462,420 |
| Dal-Tile | | | 2,298,695 | 2,257,107 |
| Unilin | | | 3,613,857 | 3,302,195 |
| Corporate and Eliminations | | | 223,226 | 156,672 |
| | | | \$ 8,527,170 | 8,178,394 |

13. Employee Benefit Plans

The Company has various pension plans covering employees in Belgium, France and the Netherlands (the "Non-U.S. Plans") that it acquired with the acquisition of Unilin Holding NV in October 2005. Benefits under the Non-U.S. Plans depend on compensation and years of service. The Non-U.S. Plans are funded in accordance with

local regulations.

Pension expense for the Non-U.S. Plans includes the following components for the three and nine months ended:

| | Non-U.S. Plans | | | |
|---|--------------------|---------------|-------------------|---------------|
| | Three months ended | | Nine months ended | |
| | September 30, | September 30, | September 29, | September 30, |
| | 2007 | 2006 | 2007 | 2006 |
| Service cost of benefits earned | \$ 470 | 402 | 1,380 | 1,205 |
| Interest cost on projected benefit obligation | 251 | 209 | 697 | 625 |
| Estimated return on plan assets | (188) | (158) | (538) | (474) |
| Net pension expense | \$ 533 | 453 | 1,539 | 1,356 |

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

The Company terminated its non-contributory defined benefit plan in October 2006 and had an obligation of \$28,472. As of September 29, 2007, approximately \$27,700 of the obligation has been paid out. During the third quarter of 2007 the Company made cash contributions of approximately \$8,700, which fully funds the plan. The Company expects to make cash contributions of \$1,485 to its Non-U.S. Plans in 2007.

14. Income Taxes

The Company adopted the provisions of FASB No. 48 ("FIN 48"), *"Accounting for Uncertainty in Income Taxes-an Interpretation of FASB Statement No. 109,"* on January 1, 2007. Upon adoption, the Company recognized no change to opening retained earnings. The Company's total balance of unrecognized tax benefits as of January 1, 2007 is approximately \$156,018, excluding any accruals for interest and penalties. Included in the balance as of January 1, 2007 is approximately \$34,151 of uncertain tax positions that, if recognized, would affect the Company's overall effective tax rate. Through the nine months ended September 29, 2007, there has not been any material change in the amount of unrecognized tax benefits.

The Company recognizes interest and penalties accrued related to unrecognized tax benefits as a component of its income tax provision. As of January 1, 2007, the Company had approximately \$47,972 accrued for the payment of interest and penalties, which does not include the federal tax benefit of interest deductions, where applicable. Through the nine months ended September 29, 2007, there has not been any material change in interest and penalties accrued to unrecognized tax benefits.

The Company files income tax returns in the U.S. federal jurisdiction and various state, local and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 1999. The Company is protesting through the IRS Appeals division the timing and deductibility of certain contingent liabilities related to the audit of its 1999 - 2001 tax

years. In connection with its protest, the Company paid a \$35,844 cash bond to the IRS; by the end of 2007, it is reasonably possible that an additional payment of approximately \$13,221 could be made. In addition, the Company believes it is reasonably possible that the balance of unrecognized tax benefits could decrease by \$61,800 within the next twelve months for individual matters of lesser amounts due to settlements or statutory expirations in various tax jurisdictions.

The Company is also under examination for tax years 2002-2003 with the IRS and in various state and foreign jurisdictions for which the anticipated adjustments would not result in a significant change to the total amount of unrecognized tax benefits.

During the third quarter of 2007, the Company's tax rate was reduced, with such reduction principally due to a greater percentage of income in lower taxed jurisdictions and changes which resulted in higher interest deductions outside the U.S. Subsequent to the third quarter, the Company began plans to implement additional changes, including a change in residency of one of its foreign subsidiaries. These changes are anticipated, subject to realization, to result in a deferred tax asset in excess of \$200,000 and a related cash benefit to be received in the future. The Company is currently evaluating the impact of these changes on its future consolidated financial statements.

15. Commitments, Contingencies and Other

The Company is involved in litigation from time to time in the regular course of its business. Except as noted below, there are no other material legal proceedings pending or known to be contemplated to which the Company is a party or to which any of its property is subject.

In *Shirley Williams et al. v. Mohawk Industries, Inc.*, four plaintiffs filed a putative class action lawsuit in January 2004 in the United States District Court for the Northern District of Georgia, alleging that they are former and current employees of the Company and that the actions and conduct of the Company, including the employment of persons who are not authorized to work in the United States, have damaged them and the other members of the putative class by suppressing the wages of the Company's hourly employees in Georgia. The plaintiffs seek a variety of relief, including (a) treble damages; (b) return of any allegedly unlawful profits; and (c) attorney's fees and costs of litigation. In February 2004, the Company filed a Motion to Dismiss the Complaint, which was denied by the District Court in April 2004. Following appellate review, the case has been returned to the District Court and discovery is proceeding.

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

In an internal review, the Company discovered that it had exchanged employee compensation information with its competitors while gathering market data. The Company discontinued this activity and voluntarily disclosed the practice to the Department of Justice. No claim has been asserted.

The Company believes that adequate provisions for resolution of all contingencies, claims and pending litigation have been made for probable losses and that the ultimate outcome of these actions will not have a material adverse effect on its financial condition but could have a material adverse effect on its results of operations in a given quarter or annual period.

The Company has received partial refunds from the United States government in reference to settling custom disputes dating back to 1982. The Company has received partial refunds totaling \$28,590 (\$18,076 net of taxes). No refunds were recorded during the three months ended September 29, 2007. For the nine months ended September 29, 2007, the Company recorded refunds of \$9,154 (\$5,812 net of taxes). The Company recorded refunds of \$8,834 (\$5,615 net of taxes) and \$15,066 (\$9,518 net of taxes) for the three and nine month periods ended September 30, 2006, respectively. Additional future recoveries will be recorded when realized.

16. Acquisitions

On August 13, 2007, the Company completed an asset purchase of four wood flooring plants from Columbia Forest Products, Inc. for \$148,760. The acquisition includes the assets of two pre-finished solid plants and one engineered wood plant in the United States and an engineered wood plant in Malaysia. In connection with the

acquisition, the Company recorded \$12,968 in goodwill. The results of operation from the date of acquisition are included in the Company's consolidated results. Net sales were approximately \$15,000 and operating income was not significant to the consolidated results for the quarter ending September 29, 2007.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

The Company is a leading producer of floor covering products for residential and commercial applications in the United States and Europe with net sales in 2006 in excess of \$7.9 billion. The Company manufactures, markets and distributes carpet, rugs, ceramic tile, hardwood, resilient, laminate and natural stone in the United States, roofing systems in Europe, and laminate flooring and wood-based panels in the United States and Europe, through various selling channels.

The Company has three reporting segments, the Mohawk segment, the Dal-Tile segment and the Unilin segment. The Mohawk segment manufactures, markets and distributes its product lines, which include carpet, rugs, pad, ceramic tile, hardwood, resilient and laminate, through its network of approximately 50 regional distribution centers and satellite warehouses using company-operated trucks, common carrier or rail transportation. The segment product lines are sold through various selling channels, which include floor covering retailers, home centers, mass merchandisers, department stores, independent distributors, commercial dealers and commercial end users. The Dal-Tile segment manufactures, markets and distributes its product lines, which include ceramic tile, porcelain tile and stone products, through its network of regional distribution centers and approximately 265 company-operated sales service centers using company-operated trucks, common carriers or rail transportation. The segment product lines are purchased by floor covering retailers, home centers, independent distributors, tile specialty dealers, tile contractors, and commercial end users. The Unilin segment manufactures, markets and distributes its product lines, which include laminate flooring, wood flooring, insulated roofing and other wood-based panels through various selling channels, which include independent retailers, home centers, independent distributors, contractors, and commercial users.

The Company reported net earnings of \$122.1 million or diluted earnings per share ("EPS") of \$1.78, down for the third quarter of 2007 compared to net earnings of \$127.7 million or \$1.88 EPS for the third quarter of 2006. Net earnings and EPS include a charge of \$14.2 million before tax (\$0.13 per share) related to plant closings in the Mohawk and Dal-Tile segments. The decrease in EPS resulted primarily from lower sales demand in the Company's U.S. residential new construction and replacement channels, which the Company believes is primarily attributable to the slowing U.S. housing industry, partially offset by a lower tax rate due to new tax strategies in Europe, continued growth in the European and commercial channels and favorable Euro exchange rates.

The Company reported net earnings of \$327.7 million or diluted EPS of \$4.79 for the first nine months of 2007 compared to net earnings of \$326.3 million, or \$4.80 EPS for the first nine months of 2006. The decrease in EPS resulted primarily from lower sales demand in the Company's U.S. residential new construction and replacement channels, which the Company believes is primarily attributable to the slowing U.S. housing industry, and plant shutdowns, offset by a lower tax rate due to new tax strategies in Europe, continued growth in the European product categories and the favorable Euro exchange rate.

Results of Operations

Quarter Ended September 29, 2007, as Compared with Quarter Ended September 30, 2006

Net sales for the quarter ended September 29, 2007 were \$1,937.7 million, reflecting a decrease of \$86.3 million, or approximately 4.3%, from the \$2,024.0 million reported in the quarter ended September 30, 2006. The decrease occurred in the Company's U.S. residential new construction and replacement channels, which the Company believes has been impacted by the slowing U.S. housing industry, offset by stronger sales within the European product categories. The Mohawk segment recorded net sales of \$1,076.7 million in the current quarter compared to \$1,233.8 million in the third quarter of 2006, representing a decrease of \$157.1 million, or approximately 12.7%. The decrease primarily arose from lower demand in its residential new construction and replacement channels, which the Company believes was impacted by the slowing U.S. housing industry, partially offset by increased sales in the commercial channels. The Dal-Tile segment recorded net sales of \$497.4 million in the current quarter, representing a decrease of \$3.8 million, or approximately 1%, compared to \$501.2 million reported in the third quarter of 2006. The decrease occurred in its residential sales channel, which the Company believes was affected by the slowing U.S. housing industry. The Unilin segment recorded

net sales of \$378.4 million in the current quarter compared to \$292.9 million in the third quarter of 2006, representing an increase of \$85.5 million, or approximately 29.2%. The increase in sales is primarily attributable to an increase in selling prices, higher demand in Europe and the U.S., favorable Euro exchange rates and the incremental impact of an acquisition during the quarter.

Gross profit for the third quarter of 2007 was \$545.4 million (28.1% of net sales) and represented a decrease of \$23.1 million from gross profit of \$568.5 million (28.1% of net sales) for the prior year's third quarter. Gross profit as a percentage of net sales in the current quarter was unfavorably impacted by plant shutdowns and lower production volume in the U.S. partially offset by price increases and higher demand in Europe.

Selling, general and administrative expenses for the third quarter of 2007 were 344.6 million (17.8% of net sales) compared to \$345.8 million (17.1% of net sales) for the prior year's third quarter. The increase in the selling, general and administrative expenses as a percentage of net sales was primarily attributable to lower sales in proportion to selling, general and administrative expenses, and higher amortization expenses, which arose from the Unilin acquisition.

Operating income for the third quarter of 2007 was \$200.8 million (10.4% of net sales) compared to \$222.7 million (11.0% of net sales) in the third quarter of 2006. Operating income as a percentage of net sales in the current quarter was unfavorably impacted by lower sales volume, which the Company believes is primarily attributable to the slowing U.S. housing industry and plant shutdowns, partially offset by higher sales in Europe. Operating income in the Mohawk segment was \$77.0 million (7.2% of segment net sales) in the third quarter of 2007 compared to \$110.5 million (9.0% of segment net sales) in the third quarter of 2006. Declining operating income as a percentage of net sales in the current quarter occurred in its residential new construction and replacement channels, which the Company believes was primarily affected by the slowing U.S. housing industry, plant shutdowns and increased manufacturing costs resulting from lower production volume, partially offset by increased sales in the commercial channels. In the Dal-Tile segment, operating income was \$63.1 million (12.7% of segment net sales) in the third quarter of 2007 compared to \$69.6 million (13.9% of segment net sales) for the third quarter of 2006. Operating income as a percentage of net sales was unfavorably impacted by its residential channel, which the Company believes is primarily attributable to the slowing U.S. housing industry and a plant shutdown. Operating income in the Unilin segment was \$71.0 million (18.8% of segment net sales) in the third quarter of 2007 compared to \$49.7 million (17.0% of segment net sales) for the third quarter of 2006. Operating income as a percentage of net sales was favorably impacted by higher selling prices and demand.

Interest expense for the third quarter of 2007 was \$37.5 million compared to \$44.7 million in the third quarter of 2006. The decrease in interest expense was directly related to lower average debt levels in the current quarter when compared to the third quarter of 2006. This decrease was partially offset by higher interest rates in the third quarter of 2007.

Income tax expense was \$42.0 million, or 25.6% of earnings before income taxes for the third quarter of 2007 compared to \$59.2 million, or 31.7% of earnings before income taxes for the prior year's third quarter. The decrease in the tax rate is principally due to a greater percentage of income in lower taxed jurisdictions and changes implemented in the third quarter of 2007 which resulted in higher interest deductions outside the U.S. The Company expects these changes to result in an effective tax rate of approximately 26% in future periods.

During the fourth quarter, the Company began plans to implement additional changes, including a change in residency of one of its foreign subsidiaries. These changes are anticipated, subject to realization, to result in a deferred tax asset in excess of \$200 million and a related cash benefit to be received in the future. The Company is currently evaluating the impact of these changes on its future consolidated financial statements.

Nine Months Ended September 29, 2007, as Compared with Nine Months Ended September 30, 2006

Net sales for the first nine months ended September 29, 2007 were \$5,778.8 million, reflecting a decrease of \$228.4 million, or approximately 3.8%, from the \$6,007.2 million reported in the nine months ended September 30, 2006. The decrease primarily occurred in the Company's U.S. residential new construction and replacement channels, which the Company believes was caused by the slowing U.S. housing industry offset by stronger sales within the European product categories. The Mohawk segment recorded net sales of \$3,237.8 million in the first nine months of 2007 compared to \$3,626.4 million in the first nine months of 2006, representing a decrease of \$388.6 million, or approximately 10.7%. The decrease was due to lower demand in its residential new construction and replacement channels which the Company believes resulted primarily from the slowing U.S. housing industry, and plant shutdowns. The Dal-Tile segment recorded net sales of \$1,469.6 million in the nine months ended September 29, 2007, representing a decrease of \$12.5 million, or approximately 1%, compared to \$1,482.1 million reported in the first nine months of 2006. The decrease was primarily attributable to lower sales within its residential channel, which the Company believes was due to the slowing U.S. housing industry. The Unilin segment recorded net sales of \$1,094.1 million reflecting an increase of \$184.8 million, or approximately 20.3%, from the \$909.3 million reported in the first nine months of 2006. The increase in sales was driven by an increase in selling prices, higher demand in Europe, favorable Euro exchange rates and an increase in patent revenues.

Gross profit for the first nine months of 2007 was \$1,625.5 million (28.1% of net sales) and represented a decrease of \$51.7 million from gross profit of \$1,677.2 million (27.9% of net sales) for the prior year's first nine months. Gross profit as a percentage of net sales for the first nine months of 2007 was favorably impacted by price increases and higher demand in Europe, partially offset by lower production volume, higher raw material costs and plant shutdowns in the U.S.

Selling, general and administrative expenses for the first nine months of 2007 were \$1,055.9 million (18.3% of net sales) compared to \$1,067.5 million (17.8% of net sales) for the prior year's first nine months. The increase in the selling, general and administrative expenses as a percentage of net sales was primarily attributable to lower sales in proportion to selling, general and administrative expenses, and higher amortization expenses, which arose from the Unilin acquisition.

Operating income for the first nine months of 2007 was \$569.6 million (9.9% of net sales) compared to \$609.7 million (10.1% of net sales) in the first nine months of 2006. Operating income as a percentage of net sales in the first nine months of 2007 was unfavorably impacted by lower sales volume, which the Company believes was primarily attributable to the slowing U.S. housing industry and plant shutdowns partially offset by higher sales in Europe. Operating income attributable to the Mohawk segment was \$185.2 million (5.7% of segment net sales) in the first nine months of 2007 compared to \$275.1 million (7.6% of segment net sales) in the first nine months of 2006. Operating income as a percentage of net sales in the first nine months of 2007 was unfavorably impacted by its residential new

construction and replacement channels, which the Company believes resulted from the slowing U.S. housing industry, increased manufacturing costs resulting from lower production volume, higher raw material costs and plant shutdowns. Operating income attributable to the Dal-Tile segment was \$196.9 million (13.4% of segment net sales) in the first nine months of 2007 compared to \$213.3 million (14.4% of segment net sales) for the first nine months of 2006. Operating income as a percentage of net sales was unfavorably impacted by its residential channel, which the Company believes resulted from the slowing U.S. housing industry and a plant shutdown. Operating income attributable to the Unilin segment was \$213.3 million (19.5% of segment net sales) in the first nine months of 2007 compared to \$149.4 million (16.4% of segment net sales) for the first nine months of 2006. Operating income as a percentage of net sales was favorably impacted by higher selling prices and demand in Europe.

Interest expense for the first nine months of 2007 was \$118.2 million compared to \$131.1 million in the first nine months of 2006. The decrease in interest expense was attributable to lower average debt, partially offset by higher interest rates in the first nine months of 2007 when compared to the first nine months of 2006.

Income tax expense was \$132.2 million, or 28.7% of earnings before income taxes for the first nine months of 2007 compared to \$160.9 million, or 33.0% of earnings before income taxes for the first nine months of 2006. The decrease in the tax rate is principally due to a greater percentage of income in lower taxed jurisdictions and changes implemented in the third quarter of 2007 which resulted in higher interest deductions outside the U.S. The Company expects these changes to result in an effective tax rate of approximately 26% in future periods.

During the fourth quarter, the Company began plans to implement additional changes, including a change in residency of one of its foreign subsidiaries. These changes are anticipated, subject to realization, to result in a deferred tax asset in excess of \$200 million and a related cash benefit to be received in the future. The Company is currently evaluating the impact of these changes on its future consolidated financial statements.

Liquidity and Capital Resources

The Company's primary capital requirements are for working capital, capital expenditures and acquisitions. The Company's capital needs are met primarily through a combination of internally generated funds, bank credit lines, term and senior notes, the sale of trade receivables and credit terms from suppliers.

Cash flows generated by operations for the first nine months of 2007 were \$601.8 million compared to \$546.2 million for the first nine months of 2006. The increase in operating cash flows for the first nine months of 2007 as compared to the first nine months of 2006 is primarily attributable to the slower build up of inventory and receivables.

Net cash used in investing activities for the first nine months of 2007 was \$240.6 million compared to \$195.0 million for the first nine months of 2006. The increase is due to higher acquisition investments during 2007 as compared to 2006 partially offset by lower capital spending. Capital spending during the remainder of 2007 for the Mohawk, Dal-Tile and Unilin segments combined, excluding acquisitions, is expected to range from \$80 million to \$100 million, and will be used primarily to purchase equipment and to add manufacturing capacity.

Net cash used in financing activities for the first nine months of 2007 was \$344.1 million compared to \$419.9 million for the same period in 2006. The primary reason for the change was the repayment of certain indebtedness offset by increased borrowings relating to the acquisition of four wood flooring plants.

At September 29, 2007, a total of approximately \$478.8 million was available under the Company's revolving credit facility. The amount used under the revolving credit facility at September 29, 2007 was \$271.2 million. The amount used under the revolving credit facility is composed of \$174.9 million of borrowings, \$55.6 million of standby letters of credit guaranteeing the Company's industrial revenue bonds and \$40.7 million of standby letters of credit related to various insurance contracts and foreign vendor commitments.

The Company has an on-balance sheet trade accounts receivable securitization agreement ("Securitization Facility"). The Securitization Facility allows the Company to borrow up to \$350.0 million based on available accounts receivable. At September 29, 2007, the Company had approximately \$270.0 million outstanding secured by trade

receivables. On July 28, 2007, the Company extended the term of the Securitization Facility until July 2008.

During April 2007, the Company repaid its \$300.0 million aggregate principal amount of its senior 6.5% notes. The Company used \$220.0 and \$80.0 million of its availability under its Securitization Facility and its revolving credit facility, respectively, to repay the 6.5% notes.

Contractual Obligations

Upon the adoption of FIN 48, the Company included accrued income tax liabilities in its contractual obligations table as disclosed in the Company's 2006 Annual Report filed on Form 10-K. As of September 29, 2007, the Company has accrued income tax liabilities of approximately \$201.1 million for income tax liabilities expected to be settled within the current fiscal year. This reflects an increase of approximately \$83.0 million from what was reported in the 2007 column of the contractual obligations table as disclosed in the Company's 2006 Annual Report filed on Form 10-K. With respect to the remaining liability of \$118.1 million, the Company cannot reasonably estimate the timing of cash settlement with respective taxing authorities and accordingly has not included the amounts in the contractual obligation table. There have been no further significant changes to the Company's contractual obligations as disclosed in the Company's 2006 Annual Report filed on Form 10-K.

Critical Accounting Policies and Estimates

Except for the income tax policy, there have been no significant changes to the Company's critical accounting policies and estimates during the period. The Company's critical accounting policies and estimates are described in its 2006 Annual Report filed on Form 10-K. The methodology applied to management's estimate for income taxes has changed due to the January 1, 2007, adoption of FIN 48, "*Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109*," which clarifies the accounting for uncertainty in income taxes. For additional information regarding the adoption of FIN 48, see Note 14 of Notes to the Condensed Consolidated Financial Statements in Part I, Item 1 of this Form 10-Q.

Recent Accounting Pronouncements

In July 2006, FASB issued FIN 48, "*Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109*," which clarifies the accounting for uncertainty in income taxes. FIN 48 prescribes a recognition threshold and measurement criteria for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance

on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The Company adopted the provisions of FIN 48 on January 1, 2007. Upon adoption, the Company recognized no change to opening retained earnings.

In September 2006, FASB issued SFAS No. 157, "*Fair Value Measurements.*" SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of financial instruments according to a fair value hierarchy. Additionally, companies are required to provide certain disclosures regarding instruments within the hierarchy, including a reconciliation of the beginning and ending balances for each major category of assets and liabilities. SFAS No. 157 is effective for the Company's fiscal year beginning January 1, 2008. The Company is currently evaluating the impact of SFAS No. 157 on its consolidated financial statements.

In September 2006, FASB issued SFAS No. 158, "*Employers' Accounting for Defined Benefit Pension and Other Post Retirement Plans-an amendment of FASB Statements No. 87, 88, 106 and 132(R).*" The Company adopted all provisions of SFAS No. 158 as of December 31, 2006, except for the measurement date provisions, which are effective for fiscal years ending after December 15, 2008. The Company does not believe the adoption of the measurement provisions of SFAS no. 158 will have a material impact on its consolidated financial statements.

In February 2007, FASB issued SFAS No. 159, "*The Fair Value Option for Financial Assets and Financial Liabilities-including an amendment of FASB Statement No. 115.*" SFAS No. 159 expands the use of fair value accounting but does not affect existing standards which require assets or liabilities to be carried at fair value. The objective of SFAS No. 159 is to improve financial reporting by providing companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. Under SFAS No. 159, a company may elect to use fair value to measure eligible items at a specified election date and report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Eligible items include, but are not limited to, accounts and loans receivable, available-for-sale and held-to-maturity securities, equity method investments, accounts payable, guarantees, issued debt and firm commitments. If elected, SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing whether fair value accounting is appropriate for any eligible items and has not estimated the impact, if any, on its consolidated financial statements.

Impact of Inflation

Inflation affects the Company's manufacturing costs, distribution costs and operating expenses. The carpet and tile industry have experienced significant inflation in the prices of raw materials and fuel-related costs beginning in the first quarter of 2004. The laminate industry has experienced moderate inflation in the prices of raw material since the beginning of 2006. For the period from 1999 through the beginning of 2004, the carpet and tile industry experienced moderate inflation in the prices of raw materials and fuel-related costs. In the past, the Company has generally been able to pass along these price increases to its customers and has been able to enhance productivity to help offset increases in costs resulting from inflation in its operations.

Seasonality

The Company is a calendar year-end company. With respect to its Mohawk and Dal-Tile segments, its results of operations for the first quarter tend to be the weakest. The second, third and fourth quarters typically produce higher net sales and operating income in these segments. These results are primarily due to consumer residential spending patterns for floor covering, which historically have decreased during the first two months of each year following the holiday season. The Unilin segment's second and fourth quarters typically produce higher net sales and earnings followed by a moderate first quarter and a weaker third quarter. The third quarter is traditionally the weakest due to the European holiday in late summer.

Forward-Looking Information

Certain of the statements in this Form 10-Q, particularly those anticipating future performance, business prospects, growth and operating strategies, proposed acquisitions, and similar matters, and those that include the words "believes," "anticipates," "forecast," "estimates" or similar expressions constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. For those statements, Mohawk claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. There can be no assurance that the forward-looking statements will be accurate because they are based on many assumptions, which involve risks and uncertainties. The following important factors could cause future results to differ: changes in industry conditions; competition; raw material prices; energy costs; timing and level of capital expenditures; integration of acquisitions; introduction of new products; rationalization of operations; litigation; and other risks identified in Mohawk's SEC reports and public announcements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's exposures to market risk have not changed significantly since December 31, 2006.

Item 4. Controls and Procedures

Based on an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report, the Company's Chief Executive Officer and Chief Financial Officer have concluded that such controls and procedures were effective for the period covered by this report. No change in the Company's internal control over financial reporting occurred during the period covered by this report that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is involved in litigation from time to time in the regular course of its business. Except as noted below, there are no other significant legal proceedings pending or known to be contemplated to which the Company is a party or to which any of its property is subject.

In *Shirley Williams et al. v. Mohawk Industries, Inc.*, four plaintiffs filed a putative class action lawsuit in January 2004 in the United States District Court for the Northern District of Georgia, alleging that they are former and current employees of the Company and that the actions and conduct of the Company, including the employment of persons who are not authorized to work in the United States, have damaged them and the other members of the putative class by suppressing the wages of the Company's hourly employees in Georgia. The plaintiffs seek a variety of relief, including (a) treble damages; (b) return of any allegedly unlawful profits; and (c) attorney's fees and costs of litigation. In February 2004, the Company filed a Motion to Dismiss the Complaint, which was denied by the District Court in April 2004. Following appellate review, the case has been returned to the District Court and discovery is proceeding.

In an internal review, the Company discovered that it had exchanged employee compensation information with its competitors while gathering market data. The Company discontinued this activity and voluntarily disclosed the practice to the Department of Justice. No claim has been asserted.

The Company believes that adequate provisions for resolution of all contingencies, claims and pending litigation have been made for probable losses and that the ultimate outcome of these actions will not have a material adverse effect on its financial condition but could have a material adverse effect on its results of operations in a given quarter or annual period.

Item 1A. Risk Factors

There have been no significant changes to the Company's risk factors as disclosed in the Company's 2006 Annual Report filed on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

None

Item 5. Other Information

None

Item 6. Exhibits

No. Description

- 10.1 Amendment to Liquidity Asset Purchase Agreement dated July 30, 2007.
- 10.2 Amendment to the Third Amended and Restated Liquidity Purchase Agreement dated July 30, 2007.
- 31.1 Certification Pursuant to Rule 13a-14(a).
- 31.2 Certification Pursuant to Rule 13a-14(a).
- 32.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MOHAWK INDUSTRIES, INC.

(Registrant)

Dated: November 7, 2007

By: /s/ Jeffrey S. Lorberbaum
JEFFREY S. LORBERBAUM
Chairman, President and
Chief Executive Officer
(principal executive officer)

Dated: November 7, 2007

By: /s/ Frank H. Boykin
FRANK H. BOYKIN
Chief Financial Officer
(principal financial officer)

