KNOLL INC
Form 10-K
March 16, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2006

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 No. 001-12907

KNOLL, INC.

(Exact name of registrant as specified in its charter)

Delaware	**13-3873847**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

1235 Water Street

East Greenville, PA 18041

(215) 679-7991

(Address, including zip code, and telephone number including area code of principal executive offices)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of each class	Name of exchange on which registered
Common Stock, par value $0.01 per share	New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: NONE

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

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨, Accelerated filer x, 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

As of June 30, 2006, the aggregate market value of the registrant s common stock held by non-affiliates of the registrant was approximately $645,425,000 based on the closing sale price as reported on the New York Stock Exchange.

As of March 9, 2007, there were 49,476,751 shares of the Registrant s common stock, par value $0.01 per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s definitive Proxy Statement for its 2007 Annual Meeting of Stockholders are incorporated by reference into Part III of this report on Form 10-K to the extent stated therein.

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PART I

Item 1. *Business*

General

We are a leading designer and manufacturer of branded office furniture products and textiles. Our commitment to innovation and modern design has yielded a comprehensive portfolio of products designed to provide enduring value and help clients shape their workplaces with imagination and vision. Our products are recognized for high quality and a sophisticated image and are targeted at the middle to upper end of the market. We sell our products primarily in North America through a direct sales force of approximately 300 professionals and a broad network of over 300 independent dealers. Our distinctive operating approach has driven industry leading operating income margins among our primary publicly-held competitors.

Since our founding in 1938, we have been recognized worldwide as a design leader within our industry. Our products are exhibited in major art museums worldwide, including more than 40 pieces in the permanent Design Collection of The Museum of Modern Art in New York. This design legacy continues to flourish today and is embodied in award winning products, including the innovative *LIFE* chair and *AutoStrada*® office furniture system. Our design excellence is complemented by a management philosophy that fosters a strong collaborative culture, client-driven processes and a lean, agile operating structure. Our employees are performance-driven and motivated by a variable incentive compensation system and broad-based equity ownership in the company. Together, these core attributes have enabled us to achieve strong financial performance and have positioned us for profitable growth.

Our management evaluates the company as one reporting segment in the office furniture industry. For further information on segment reporting, see note 16 in the accompanying financial statements.

Products

We offer a comprehensive and expanding portfolio of high quality office furniture, textiles and leather across five product categories: (i) office systems, which are typically modular and moveable workspaces with functionally integrated panels, work surfaces, desk components, pedestal and other storage units, power and data systems and lighting; (ii) specialty products, including high image side chairs, sofas, desks and tables for the office and home, textiles, accessories and leathers and related products; (iii) seating; (iv) files and storage; and (v) desks, casegoods and tables. Historically, we have derived most of our revenues from office systems, work surfaces, storage and lighting, and from specialty products, including our *KnollStudio*® collection of signature design classics furnishings, *KnollTextiles* , *Spinneybeck*® leather and *KnollExtra*® accessories. However, in recent years, we have significantly expanded our product offerings in seating, files and storage, desks and casegoods and tables. Our products and knowledgeable sales force have generated strong brand recognition and loyalty among architects, designers and corporate facility managers, all of whom are key decision makers in the office furniture purchasing process. Our clients are typically Fortune 1000 companies, governmental agencies and other medium to large sized organizations in a variety of industries. We have an over $7 billion installed base of office systems, which provides a strong platform for recurring and add-on sales of products across all our categories.

Major product categories and lines include:

Systems Furniture

We believe that office systems purchases are divided primarily between (i) architect and designer-oriented products and (ii) entry-level products with technology, ergonomic and functional support. Our office systems furniture reflects the breadth of these sectors with a variety of planning models and a corresponding depth of product features. Our systems furniture can define or adapt to virtually any office environment from collaborative spaces for team interaction to private executive offices.

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Systems furniture consists principally of functionally integrated panels, work surfaces, desk components, pedestal and other storage units, power and data systems and lighting. These components are combined to create flexible, space-efficient work environments that can be moved, re-configured and re-used. Clients, often working with architects and designers, have the opportunity to select from a palette of laminates, paints, veneers and textiles to design workspaces appropriate to their organizations personality. Our systems furniture product development strategy aims to insure that product line enhancements can be added to clients existing installations, maximizing the value of the clients investments in Knoll systems products.

Office systems furniture accounted for approximately 56.5% of sales in 2006, 56.8% of sales in 2005 and 57.0% of sales in 2004.

Our systems furniture product lines include the following panel and desk-based planning models:

AutoStrada®

AutoStrada, which we began shipping in the second half of 2004, is one of the most comprehensive office concepts that we have developed. *AutoStrada* provides aesthetic and functional alternatives to traditional panel-based and desk-based systems furniture with four planning models that combine high-performance furniture with the look of custom millwork. The *AutoStrada* spine-based, storage-based, wall-based and collaborative/open table planning models leverage a consistent design aesthetic to create a distinctively modern office environment. Whether an office requires a high performance open plan system, architectural casegoods, progressive private office furniture or a collaborative big table concept, *AutoStrada* provides a solution. *AutoStrada* received a silver 2004 *Best of NeoCon®* award.

Reff ®

Reff is our flagship wood systems furniture platform. It combines the high performance capabilities of panel-based systems furniture and the refined elegance of wood casegoods, showcasing sophisticated all-wood construction and precisely crafted detail. *Reff* is available in an extensive range of veneers, durable laminates and metal options that can be used interchangeably in panel-based open areas as well as in private offices, as freestanding casegoods. *Reff* offers clients a variety of flexible panel types, making it easy to create virtually any type of workstation and has extensive power and data management capabilities for data and communications technology.

Currents®

Our award-winning and innovative *Currents* system provides advanced power and data capabilities to organizations that require maximum space-planning freedom, advanced technology support and require the mobility of freestanding furniture. The groundbreaking *Currents* service wall divides space and manages technology. *Currents* may be used in tandem with existing systems furniture, removing the constraints imposed by conventional panel systems. *Currents* also integrates with competitors systems and freestanding furniture.

Morrison

Our *Morrison* furniture system, which meets essential power and data requirements for panel and desk-based planning and private offices, offers one of the broadest ranges of systems performance in the industry. *Morrison* 120-degree panel-based planning extends the *Morrison* legacy of systems planning flexibility through a definitive vocabulary of universal systems components. *Morrison* has been upgraded continually with interchangeable enhancements from its *Morrison Network, Morrison Access* and *Morrison Options* lines. In addition, *Morrison* integrates with *Currents* to provide advanced wire management capabilities, as well as with our *Calibre* and *Series 2* desks, pedestals, lateral files, overhead storage cabinets and architectural towers to provide compatible, cost-effective panel and desk-based solutions.

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Equity®

The distinguishing feature of our *Equity* product is its unique centerline modularity, which maximizes the efficient use of space for high-density workplaces with a minimal inventory of parts. *Equity* incorporates power and data capabilities, including desktop features, and integrates with *Currents*, which is described above, to provide advanced wire management capabilities. *Equity* components also create modular freestanding desks, and *Equity* 120-degree planning enables clients to create sleek, hexagonal configurations that are well suited for call and data centers. For both 90- and 120-degree *Equity* planning, a variety of components accommodate clients needs for privacy and storage: add-on screens, bi-fold doors and side-door components. Add-on screens are available in perforated steel, polycarbonate, Plexiglas® and *Imago* to accommodate various aesthetic and budgetary requirements. *Equity* continues to be a leader the industry in terms of sustainable design.

Dividends®

Our *Dividends* product is a straightforward, versatile frame-and-tile furniture system featuring a universal panel frame. Removable panel inserts, which can be ordered in fabric, steel, glass or as marker boards, meet a range of clients design and budgetary needs. The *Dividends* panel frame enables clients to utilize either monolithic, tiled or beltway panel type for applications throughout the workplace, and power and data access may be located virtually anywhere on the panel. The panel, in combination with the universal post, makes the *Dividend*s system easy to re-configure, and workstations do not have to be disassembled to make changes to the panel. *Dividends* accommodates off-module planning, encouraging workstation design flexibility as well as the placement of freestanding *Dividends* desk components.

Seating

We continuously research and assess the general landscape of the office seating market, and tailor work chair product development initiatives to enhance our competitive position for ergonomics, aesthetics, comfort and value. We believe that the result of these efforts is an increasingly innovative, versatile seating collection consistent with the Knoll brand.

Key client criteria in work chair selection include superior ergonomics, aesthetics, comfort, quality and affordability, all of which is consistent with our strengths and reputation. We believe that we offer an excellent and fully competitive line up of chairs at a range of price points and performance levels and constructed from varying materials, including mesh, plastic and upholstery.

Our seating product lines are designed and engineered for clients in businesses of all sizes who seek distinctive, comfortable, high performance executive, task, conference and visitor chairs. The *LIFE*, *RPM*®*, Sapper, Bulldog*®, *SOHO* , *Visor* , *Chadwick* , and *Essentials* product lines offer a range of ergonomic features at various price levels.

In January 2006, we introduced our *Essentials* chair collection designed by Jeffrey Bernett, and in 2005 we introduced the *Chadwick* product line designed by Don Chadwick. Both of these work chair offerings target the middle-market and entry price segment.

Seating accounted for approximately 10.7% of sales in 2006, 10.4% of sales in 2005 and 9.8% of sales in 2004.

Our principal seating lines are:

LIFE . *LIFE*, introduced in 2002, has become an industry benchmark for ergonomic and sustainable design. Recognized for its overall lightness and agility, *LIFE* features intuitive adjustments that bring comfort and effortless control to a new performance level with an extensive range of supportive sitting options and responsive lumbar support.

RPM. *RPM*, recognized for outstanding comfort, extraordinary performance and exceptional value, is offered with distinctive fabrics that reflect its stylish design. Engineered for durability, *RPM* delivers comfort and support, especially for 24-hour work environments.

Chadwick . *Chadwick*, introduced in 2005, is an innovative hybrid seating design that accommodates the changing needs of today s workplace and home office.

Essentials . *Essentials*, introduced in January 2006, is a traditional, tailored, practical work chair designed to offer the ergonomic comfort and traditional appeal of fully upholstered task chair at an incredible value. *Essentials* Work Chairs, with two models, Pro and Tech , are a comprehensive range of three task and two side chairs suitable to any office style from the traditional to the progressive.

Files and Storage

Our files and storage products, featuring the *Calibre* and *Series 2* product lines, are designed with unique features to maximize storage capabilities throughout the workplace. Our core files and storage products consist of lateral files, mobile pedestals and other storage units, bookcases and overhead storage cabinets. In 2004, the breadth of our storage products was expanded by introducing new storage towers, including wardrobe towers, bookcase towers and display towers. Knoll *Calibre* storage towers received a silver 2004 *Best of NeoCon*® award.

The range of files and storage completes our product offering, allowing clients to address all of their furniture needs with us, especially in competitive bid situations where Knoll office systems, seating, tables and desks have been specified. The breadth of the product line also enables our dealers to offer the files and storage as stand alone products to businesses with smaller requirements.

Files and storage are available in an extensive array of sizes, configurations and colors, which can be integrated with other manufacturers stand-alone furniture, thereby increasing our penetration in competitor accounts. In addition, certain elements of the product line can be configured as freestanding furniture in private offices or open-plan environments.

Files and storage accounted for approximately 8.3% of sales in 2006, 7.3% of sales in 2005 and 7.3% of sales in 2004.

Desks, Casegoods, and Tables

We offer collections of adjustable tables as well as meeting, conference, training, dining, and café tables for large scale projects and stand-alone desks and table desks. These items are also sold as stand-alone products through Knoll dealers to businesses with smaller requirements.

Our *Interaction* and *Upstart* product lines include adjustable, work, meeting, conference and training tables. These product lines range from independent tables to tables suitable for workstations that support individual preferences for computer and writing heights to plannable desks that can be linked together to build and reshape larger work areas. Additionally, *Interaction* tables are designed to be compatible with *Dividends*, *Equity*, *Morrison* and *Reff* office systems.

Our principal desk product lines, detailed to meet the needs of the contemporary office, offer traditional wood casegoods construction synonymous with the Knoll standard of quality. These desk product lines include: *Magnusson*® and *Reff*®, both designed especially to serve the day-to-day wood casegoods requirements of Knoll dealers.

Desks, Casegoods, and Tables accounted for approximately 0.5% of sales in 2006, 0.9% of sales in 2005 and 1.5% of sales in 2004.

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Specialty Products

Our *KnollStudio*®, *KnollTextiles*, *KnollExtra*® and *Spinneybeck*® businesses serve as a marketing and distribution umbrella for our portfolio of specialty product lines. These businesses, which represented over 16% of our revenue in 2006, are our highest margin product lines and enhance our design and quality reputation.

KnollStudio is a renowned source for classic modern furniture and spirited new designs of unparalleled quality for the workplace, home, hotels, restaurants and government and educational institutions. The *KnollStudio* portfolio includes a range of lounge seating; side, café and dining chairs; barstools; and conference, dining and occasional tables. *KnollStudio* has a long history of working with celebrated architects and designers from around the world, including Ludwig Mies van der Rohe, Marcel Breuer, Eero Saarinen, Isamu Noguchi, Warren Platner, Frank Gehry, Maya Lin, Jens Risom and Kazuhide Takahama. In addition, *KnollStudio* manufactures a collection of original furniture designs by Florence Knoll. In 2006, *KnollStudio* collaborated with renowned New York-based architectural firm Shelton, Mindel & Associates to produce a range of elegant lounge seating, an innovative wood side chair and a series of low tables.

In the fourth quarter of 2004, *KnollStudio* established *Knoll Space* as a formalized sales program for the retail market, making it easier for consumers to bring the best of Knoll furnishings into their home and home office. The program consists of independent specialty retailers and e-tailers nationwide that sell our iconic modern classics and selected contemporary designs as well as selected products with crossover home office appeal. Through this program we sell our *KnollStudio* and selected other products through approximately 50 retailers, with an aggregate of over 100 locations.

KnollTextiles, established in 1947 to create high-quality textiles for Knoll furniture, offers upholstery, panel fabrics, wall coverings and drapery that harmonize color, pattern and texture. *KnollTextiles* offers products for corporate, hospitality, healthcare and residential interiors. *KnollTextiles* products are used in the manufacture of Knoll furniture and are sold to clients for use in other manufacturers products. Extending *KnollTextiles* heritage of product innovation from classic upholstery to ecologically oriented panel fabrics; we introduced *Imago* in 2000, a product that defined an entirely new category of hard surface materials. Designers who collaborate with us on *KnollTextiles* include Suzanne Tick and 2x4. In January 2006, *KnollTextiles* partnered with Toray to be the exclusive contract distributor for *Ultrasuede*® fabrics in the United States, for corporate, hospitality, and healthcare applications. *Ultrasuede* has been used in the fashion and automotive industries for three decades due to its unique combination of luxury and performance. This partnership reflects are commitment to classic luxury and quality. Also in 2006, *Knoll Textiles* received two *Best of NeoCon*® awards, one for *KnollTextiles* design director Dorothy Cosonas s Spring 2006 Collection in the Upholstery category, and one for Suzanne Tick s *Hard Rock and Palladium* in the Panel Fabric category.

KnollExtra offers accessories that complement Knoll office furniture products, including technology support accessories, desktop organizational tools, lighting and storage. *KnollExtra* integrates technology comfortably into the workplace, meeting the increased demand for flat panel monitor supports, central processing unit holders as cable management with such products as *Zorro*, *Wishbone* and *Rotation*, which deliver adjustability and space savings. In 2005, our portable, aluminum, ergonomic support for laptop computers *Lapjack* won a gold 2005 *Best of NeoCon*® award. In addition we received the silver and gold 2005 *Best of NeoCon*® awards for the Copeland Light and the Halley Light.

Spinneybeck Enterprises, Inc. (Spinneybeck), our wholly owned subsidiary, offers leathers and related products, including leather rugs and wall panels. *Spinneybeck* supplies high-quality upholstery leather for use on Knoll furniture and for sale directly to clients, including other office furniture manufacturers, upholsterers, aviation, custom coach and boating manufacturers.

Specialty products accounted for approximately 16.2% of sales in 2006, 16.6% of sales in 2005 and 16.5% of sales in 2004.

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European Products

Knoll Europe has a product offering that allows clients to purchase a complete office environment from a single source. In addition, we offer certain products designed specifically for the European market. In 2006 we introduced the new *wa* desking system. *Wa* reinvents desks and storage through its design and construction in a linear and well proportioned modern vernacular. Our presence in the European market provides strategic positioning with clients that have international offices where they would like to maintain their Knoll facility standard. In addition to working with North American clients international offices, we also have a local European client base.

In Europe, the core product categories include: (i) desk systems, including the new *wa* desking system the *KnollScope,* and the *PL1* system; (ii) *KnollStudio*; (iii) seating, including a comprehensive range of chairs; and (iv) storage units, which are designed to complement Knoll desk products.

Knoll Europe accounted for approximately 7.8% of sales in 2006 and in 2005 and 7.7% of sales in 2004.

Product Design and Development

Our design philosophy reflects our historical commitment to working with the world s preeminent designers to develop products and product enhancements that delight and inspire. By combining the designers creative vision with our commitment to developing products that address changing business needs, we have been able to generate strong demand for our product offerings and cultivate brand loyalty among target clients. Our reputation as a design leader and history of working with these preeminent designers allows us to continue to attract and collaborate with a diverse group of the world s leading designers. In addition, these types of collaborations are consistent with our commitment to a lean organizational structure and incentive-based compensation, with the resulting costs a variable royalty-based fee as opposed to fixed costs associated with a larger in-house design staff.

Our product development process uses a product commercialization process to ensure quality and repeatability of the development process. This helps to reduce product development cycle time and improves the quality of output. We use Pro/ENGINEER® design tools and rapid prototyping technology to reduce product design and development lead times and improve responsiveness to special requests for customized solutions. Working very closely with the designers during this phase of design and development helps to ensure the most viable products that balance innovative, modern design with practical, functional style. Cross-functional teams are formed for all major development efforts with dedicated leaders to facilitate a seamless flow into manufacture and accountability on cost and schedule. Additionally, throughout the development process, materials that are used are evaluated with a focus on incorporating recycled and recyclable materials into the products.

Research and development expenses, which are expensed as incurred, were $12.7 million for 2006, $10.8 million for 2005, and $12.8 million for 2004.

Sales and Distribution

Our clients are typically Fortune 1000 companies, governmental agencies and other medium to large sized organizations in a variety of industries including education, healthcare and hospitality. Our direct sales force and independent dealers in North America work in close partnership with clients and design professionals to specify distinctive work environments. Our direct sales representatives, in conjunction with the independent dealers, sell to and call directly on key clients. Our independent dealers also call on many other medium and small sized clients to provide seamless sales support and client service.

Our products and knowledgeable sales force have generated strong brand recognition and loyalty among architects, designers and corporate facility managers, all of whom are key decision makers in the office furniture purchasing process. Our strong relationships with architects and design professionals help us stay abreast of key

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workplace trends and position us to better meet the changing needs of clients. For example, we have invested in training all of our architect and designer specialists as Leadership in Energy and Environmental Design (LEED®) accredited professionals to help clients better address environmental issues that arise in the design of the workplace. We have over $7 billion installed base of office systems, which provides a strong platform for recurring and add-on sales.

We have aligned our sales force to target strategic areas of opportunity. For example, our Global Business Division was created to target competitively held accounts. We have also placed sales representatives and technical specialists into certain dealerships to support programs such as *Knoll Essentials*, as well as strengthened our focused seating and *KnollExtra* sales team with new senior leadership.

In addition to coordinating sales efforts with the sales representatives, the dealers generally handle project management, installation and maintenance for client accounts after the initial product selection and sale. Although many of these dealerships also carry products of other manufacturers, they have agreed not to act as dealers for our principal direct competitors. We have not experienced significant dealer turnover. Our dealers substantial commitment to understanding our product lines, and their strong relationships with us, serve to discourage dealers from changing vendor affiliations. We are not dependent on any one dealer, the largest of which accounted for less than 8.2%, 7.2% and 5.2% of our North American sales in 2006, 2005 and 2004, respectively.

We provide product training for our sales force and dealer sales representatives, who make sales calls primarily to small to medium sized businesses. As part of our commitment to building relationships with our dealer sales representatives, we introduced the *Knoll Essentials* program in January 2004. *Knoll Essentials* is a catalog program developed in response to dealer requests for a consolidated, user-friendly selling tool for day-to-day systems, seating, storage and accessory products. The *Knoll Essentials* program includes dealer incentives to sell our products. In 2006, the *Knoll Essentials* program increased dealer generated sales by $19.0 million as compared to 2005. We also employ a dedicated team of dealer sales representatives to work with our dealerships.

No single client represented more than 2.6% of our North American sales during 2006. However, a number of U.S. government agencies purchase products through multiple contracts with the General Services Administration, or GSA. Sales to U.S. government entities under the GSA contracts aggregated approximately 12.6% of our consolidated sales in 2006, with no single U.S. government order accounting for more than 2% of consolidated sales. The U.S. government typically can terminate or modify any of its contracts with us either for its convenience or if we default by failing to perform under the terms of the applicable contract.

In Europe, we sell products in largely the same manner as in North America, through a direct sales force and a network of dealers with the majority of sales coming from the United Kingdom, France and Italy, as well as export markets in the Middle East. We also sell products designed and manufactured in North America to the international operations of core clients.

Manufacturing and Operations

We operate manufacturing sites in North America, with plants located in East Greenville, Pennsylvania, Grand Rapids and Muskegon, Michigan, and Toronto, Canada. In addition, we have two plants in Italy: one in Foligno and one in Graffignana. We manufacture and assemble products to specific customer order and operate all facilities under a philosophy of continuous improvement, lean manufacturing and efficient asset utilization. All plants are registered under ISO 9000, an internationally developed set of quality criteria for manufacturing companies. Additionally, the North American plants are ISO 14001 certified, which reflects our commitment to environmentally responsible practices.

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In 2006, our East Greenville location received a Star rating under the Occupational Safety and Health Administration s (OSHA) Voluntary Protection Program (VPP). A Star rating is the highest a company can obtain in OSHA s premier partnership program and to achieve this rating our East Greenville site had to demonstrate a comprehensive safety and health process with strong management leadership, include all employees as active participants and ensure an injury rate substantially below the average for the industry. The Star rating allows us to join an elite and exclusive group of less than 1,400 companies nationwide that have demonstrated the dedication and commitment to safety.

The root of our continuous improvement efforts lies in the philosophy of lean manufacturing that drives operations. As part of this philosophy, we partner with suppliers who can supply our facilities efficiently, often with just-in-time deliveries, thus allowing us to reduce our raw materials inventory. We also utilize Kaizen work groups in the plants to develop best practices to minimize scrap, time and material waste at all stages of the manufacturing process. The involvement of employees at all levels ensures an organizational commitment to lean and efficient manufacturing operations.

In 2006, we encountered capacity restraints as the industry continued its recovery and we worked to meet the increased demand for our product. To respond to this issue, we added additional shifts and invested in new equipment. These steps allowed us to increase capacity without entering into new facilities or enlarging our existing facilities. In addition, the increased demands presented challenges in receiving our inbound materials and shipping orders to customers on time. To correct this issue we incurred additional costs to expedite the shipments in and out of our facilities. By the end of the year, these challenges had been addressed and are, we believe, behind us. But we continue to implement new programs and procedures which will improve operations from order entry through shipment, resulting in more efficient workflows, reduced lead times and enhanced client service. We continue to focus on process cycle time, percentage of orders shipped complete and on-time, order correctness and other key measures aimed at driving service improvements.

In addition to the continued focus on enhancing the efficiency of the manufacturing operations, we also seek to reduce costs through our recently initiated global sourcing effort. We have capitalized on raw material and component cost savings available through lower cost global suppliers. This broader view of potential sources of supply has enhanced our leverage with domestic supply sources, and we have been able to reduce cycle times by extracting improvements from all levels throughout the supply chain.

Raw Materials and Suppliers

The purchasing function in North America is centralized at the East Greenville facility. This centralization, and the close relationships with our primary suppliers, has enhanced our ability to realize purchasing economies of scale and implement just-in-time inventory practices. Steel, lumber, paper, paint, plastics, laminates, particleboard, veneers, glass, fabrics, leathers and upholstery filling material are used in the manufacturing process. Both domestic and overseas suppliers of these materials are selected based upon a variety of factors, with the price and quality of the materials and the supplier s ability to meet delivery requirements being primary factors in such selection. We do not generally enter into any long-term supply contracts and, as a result, we are vulnerable to fluctuations in the prices for these materials. Our material costs increased by approximately $12.8 million during 2006 due to increasing market prices. In 2006, inflation impacted transportation costs by $1.9 million. The existing and ongoing global sourcing initiative and continuous improvement program, implemented list price increases and selected additional list price increases are anticipated to offset most of these further increased material costs; however the additional impact of transportation inflation will make it more difficult for us to offset all of these costs. No supplier is the only available source for a particular component or raw material. However, because of the specialization involved with some of our components, it can take a significant amount of time and effort to move to an alternate source.

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Competition

The office furniture market is highly competitive. Office furniture companies compete on the basis of (i) product design, including performance, ergonomic and aesthetic features, (ii) product quality and durability, (iii) relationships with clients, architects and designers, (iv) strength of dealer and distributor network, (v) on-time delivery and service performance, (vi) commitment to environmental standards by offering products that help clients achieve LEED® certified facilities and minimize environment impact and (vii) price. We estimate that we had an 8.3% market share in the U.S. office furniture market in 2006.

Some of our competitors, especially those in North America, are large and have significantly greater financial, marketing, manufacturing and technical resources than we have. Our most significant competitors in primary markets are Herman Miller, Inc., Steelcase, Inc., Haworth, Inc. and, to a lesser extent, Allsteel, Inc., an operating unit of HNI Corporation and Teknion Corporation. These competitors have a substantial volume of furniture installed at businesses throughout North America, providing a continual source of demand for further products and enhancements. Moreover, the products of these competitors have strong acceptance in the marketplace. Although we believe that we have been able to compete successfully in the markets to date, there can be no assurance that we will be able to continue to do so in the future.

Patents and Trademarks

We consider securing and protecting our intellectual property rights to be important to the business. We own approximately 82 active U.S. utility patents on various components used in our products and systems and approximately 107 active U.S. design patents. We also own approximately 190 patents in various foreign countries. The scope and duration of our patent protection varies throughout the world by jurisdiction and by individual product. In particular, patents for individual products extend for varying periods of time according to the date a patent application is filed, the date a patent is granted and the term of patent protection available in the jurisdiction granting the patent (generally twenty years from the date of filing in the U.S, for example). We believe that the duration of the applicable patents we are granted is adequate relative to the expected lives of our products. We own approximately 46 trademark registrations in the U.S., including registrations to the following trademarks, as well as related stylized depictions of the Knoll word mark: Knoll®, KnollStudio®, KnollExtra®, Good Design Is Good Business®, A3®, Autostrada®, Bulldog®, Calibre®, Currents®, Dividends®, Equity®, Parachute®, Propeller®, Reff®, RPM®, Spinneybeck®, Upstart®, Visor®. We also own approximately 143 trademarks registered in foreign countries including the LIFE trademark which was purchased in December 2006. The scope and duration of our trademark protection varies throughout the world, with some countries protecting trademarks only as long as the mark is used, and others requiring registration of the mark and the payment of registration (generally ten years from the date of filing in the U.S., for example). In order to protect the indefinite duration, we makes filings to continue registration of our trademarks.

In October 2004, we received registered trademark protection in the United States for five of our world-famous furniture designs created by Ludwig Mies van der Rohe the Barcelona Chair, the Barcelona Stool, the Barcelona Couch, the Barcelona Table and the Flat Bar Brno Chair. This protection recognizes the renown of these designs and reflects our commitment to ensuring that when architects, furniture retailers, businesses and the public purchase a Ludwig Mies van der Rohe design, they will be purchasing the authentic product, manufactured to the designer s historic specifications. Barcelona® is a U.S. registered trademark owned by Knoll, Inc.

Backlog

Our sales backlog was $167.7 million at December 31, 2006, $147.3 million at December 31, 2005 and $122.5 million at December 31, 2004. We manufacture substantially all of our products to order and expect to fill substantially all outstanding unfilled orders within the next twelve months. As such, backlog is not a significant factor used to predict our long-term business prospects.

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Foreign and Domestic Operations

Our principal manufacturing operations and markets are in North America, and we also have manufacturing operations and markets in Europe. Our sales to clients and net property, plant and equipment are summarized by geographic areas below. Sales to clients are attributed to the geographic areas based on the point of sale.

	United States	Canada	Europe	Consolidated
		(in thousands)		
2006				
Sales to clients	$ 870,713	$ 33,216	$ 78,223	$ 982,152
Property, plant and equipment, net	88,105	35,513	14,111	137,729
2005				
Sales to clients	$ 715,453	$ 29,490	$ 63,017	$ 807,960
Property, plant and equipment, net	95,074	35,070	12,022	142,166
2004				
Sales to clients	$ 633,787	$ 18,192	$ 54,411	$ 706,390
Property, plant and equipment, net	103,225	33,722	14,045	150,992

Environmental Matters

We believe that we are substantially in compliance with all applicable laws and regulations for the protection of the environment and the health and safety of our employees based upon existing facts presently known to us. Compliance with federal, state, local and foreign environmental laws and regulations relating to the discharge of substances into the environment, the disposal of hazardous wastes and other related activities has had and will continue to have an impact on our operations, but has, since 1990, been accomplished without having a material adverse effect on our operations. There can be no assurance that such laws and regulations will not change in the future or that we will not incur significant costs as a result of such laws and regulations. We have trained staff responsible for monitoring compliance with environmental, health and safety requirements. Our goal is to reduce and, wherever possible, eliminate the creation of hazardous waste in our manufacturing processes. While it is difficult to estimate the timing and ultimate costs to be incurred due to uncertainties about the status of laws, regulations and technology, based on information currently known to management, we do not expect environmental costs or contingencies to have a material adverse effect on our consolidated financial position, results of operations or cash flows. The operation of manufacturing plants entails risks in these areas, however, and we cannot be certain that we will not incur material costs or liabilities in the future which could adversely affect our operations.

We have been identified as a potentially responsible party pursuant to the Comprehensive Environmental Response Compensation and Liability Act, or CERCLA , for remediation costs associated with waste disposal sites previously used by us. CERCLA can impose liability for costs to investigate and remediate contamination without regard to fault or the legality of disposal and, under certain circumstances, liability may be joint and several resulting in one responsible party being held responsible for the entire obligation. Liability may also include damages for harm to natural resources. The remediation costs and our allocated share at some of these CERCLA sites are unknown. We may also be subject to claims for personal injury or contribution relating to CERCLA sites. We would reserve amounts for such matters when expenditures are probable and reasonably estimable.

Employees

As of December 31, 2006, we employed a total of 4,224 people, consisting of 2,930 hourly and 1,294 salaried employees. The Grand Rapids, Michigan plant is the only unionized plant within the U.S and has an agreement with the Carpenters Union, Local 1615, of the United Brotherhood of Carpenters and Joiners of America, Affiliate of the Carpenters Industrial Council (the Union), covering approximately 418 hourly employees. The previous collective bargaining agreement was effective through August 27, 2006. On August 25,

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2006, we entered into a new five-year collective bargaining agreement with the Union covering bargaining unit members at the Grand Rapids, Michigan facility. The new collective bargaining agreement was ratified on August 25, 2006 and became binding at that time. The collective bargaining agreement sets forth the terms and conditions of employment for bargaining unit members working at our Grand Rapids, Michigan facility and became effective on August 27, 2006, upon expiration of the previous agreement. The Collective Bargaining Agreement continues until August 27, 2011. From time to time, there have been unsuccessful efforts to unionize at our North American locations. We believe that relations with our employees throughout North America are good. Nonetheless, it is possible that our employees may continue attempts to unionize. Certain workers in the facilities in Italy are also represented by unions. We have experienced brief work stoppages from time to time at our plants in Italy, none of which have exceeded eight hours. Work stoppages are relatively common occurrences at many Italian manufacturing plants and are usually related to national or local issues. We had 4 such work stoppages in 2006, with an average duration of 5.2 hours. None of these work stoppages were unique to us, and these work stoppages have not materially affected our performance.

Available Information

Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports are made available free of charge through the Investors Relations section of our website at www.knoll.com, as soon as practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission.

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Item 1A. ***Risk Factors***

RISK FACTORS

Our product sales are tied to corporate spending and service-sector employment, which are outside of our control. Our sales and/or growth in sales would be adversely affected by a recessionary economy characterized by decreased corporate spending and service-sector employment.

Our sales are significantly impacted by the level of corporate spending primarily in North America, which, in turn, is a function of the general economic environment. In a recessionary economy, service-sector employment, corporate cash flows and non-residential commercial construction decrease, which typically leads to a decrease in demand for office furniture. In addition, a recessionary economy may also result in saturation of the market by just new used office systems, leading to a decrease in demand. Sales of office systems, which have historically accounted for more than half of our revenues, represent longer term and higher cost investments for our clients. As a result, sales of office systems are more severely impacted by decreases in corporate spending than sales of seating, files and storage and casegoods, and demand for office systems typically takes longer to respond to an economic recovery.

Geopolitical uncertainties, terrorist attacks, acts of war, natural disasters, increases in energy and other costs or combinations of such and other factors that are outside of our control could at any time have a significant effect on the North American economy, and, therefore, our business. The occurrence of any of these or similar events in the future could result in downward pressure on the economy, which we would expect to cause demand for our products to decline and competitive pricing pressures to increase.

We may have difficulty increasing or maintaining our prices as a result of price competition, which could lower our profit margins. Our competitors may develop new product designs that give them an advantage over us in making future sales.

Office furniture companies compete on the basis of, among other things, price and product design. Since our competitors offer products that are similar to ours, we face significant price competition from our competitors, which tends to intensify during an industry downturn. This price competition impacts our ability to implement price increases or, in some cases, such as during an industry downturn, maintain prices, which could lower our profit margins. Additionally, our competitors may develop new product designs that achieve a high level of customer acceptance, which could give them a competitive advantage over us in making future sales.

Our efforts to introduce new products that meet customer and workplace requirements may not be successful, which could limit our sales growth or cause our sales to decline.

To keep pace with workplace trends, such as changes in workplace design and increases in the use of technology, and with evolving regulatory and industry requirements, including environmental, health, safety and similar standards for the workplace and for product performance, we must periodically introduce new products. The introduction of new products requires the coordination of the design, manufacturing and marketing of such products, which may be affected by factors beyond our control. The design and engineering of certain of our new products can take up to a year or more, and further time may be required to achieve client acceptance. In addition, we may face difficulties in introducing new products if we cannot successfully align ourselves with independent architects and designers who are able to design, in a timely manner, high quality products consistent with our image. Accordingly, the launch of any particular product may be later or less successful than originally anticipated by us. Difficulties or delays in introducing new products or lack of customer acceptance of new products could limit our sales growth or cause our sales to decline.

We may not be able to manage our business effectively if we are unable to retain our experienced management team or recruit other key personnel.

The success of our operations is highly dependent upon our ability to attract and retain qualified employees and upon the ability of our senior management and other key employees to implement our business strategy. We believe there are only a limited number of qualified executives in the industry in which we compete. We rely substantially upon the services of Andrew B. Cogan, our Chief Executive Officer, and Kathleen G. Bradley, our President and Chief Executive Officer, Knoll, North America. The loss of the services of either of these individuals or other key members of our management team could seriously harm our efforts to successfully implement our business strategy.

While we currently maintain key person life insurance policies with respect to Mr. Cogan and Ms. Bradley, this insurance may not be sufficient to compensate us for any harm to our business resulting from loss of their services. The inability to attract and retain other talented personnel could also affect our ability to successfully implement our business strategy.

We are dependent on the pricing and availability of raw materials and components, and price increases and unavailability of raw materials and components could lower sales, increase our cost of goods sold and reduce our profits and margins.

We require substantial amounts of raw materials, which we purchase from outside sources. Steel, plastics and wood related materials are the main raw materials used in the manufacture of our products. The prices and availability of raw materials are subject to change or curtailment due to, among other things, the supply of, and demand for, such raw materials, changes in laws or regulations, including duties and tariffs, suppliers allocations to other purchasers, interruptions in production by raw materials or component parts suppliers, changes in currency exchange rates and worldwide price levels.

The price of steel and plastics, the latter of which is sensitive to the cost of oil, has significantly increased in recent years. To date, we have been successful in largely offsetting these recent price increases in raw materials through our global sourcing initiatives, primarily from China, Taiwan, Italy and Germany, through our continuous improvement programs and through price increases to our products. However, if the prices of these raw materials continue to increase, we may be unable to continue to offset any further increased costs and our profit margins could be negatively affected.

In addition, contracts with most of our suppliers are short-term contracts. These suppliers may not continue to provide raw materials and components to us at attractive prices or at all, and we may not be able to obtain the raw material we need in the future from these or other providers on the scale and within the time frames we require. Moreover, we do not carry significant inventories of raw materials, components or finished goods that could mitigate an interruption or delay in the availability of raw materials and components. Any failure to obtain raw materials and components on a timely basis, or any significant delays or interruptions in the supply of raw materials, could prevent us from being able to manufacture products ordered by our clients in a timely fashion, which could have a negative impact on our reputation and our dealership network, and could cause our sales to decline.

We are affected by the cost of energy and increases in energy prices could reduce our margins and profits.

The profitability of our operations is sensitive to the cost of energy through our transportation costs, the cost of petroleum-based materials, like plastics, and the cost of operating our manufacturing facilities. Energy costs have increased in the recent years due to changes in global supply and demand. Although we have been successful in countering these recent energy price increases, primarily through our global sourcing initiatives and continuous improvement programs, we may not be able to continue to offset such costs at current price levels, or if these prices continue to increase. If the price of petroleum-based products, the cost of operating our manufacturing facilities or our transportation costs continue to increase, it could have a negative impact on our gross margins and profitability.

We rely upon independent furniture dealers, and a loss of a significant number of dealers could affect our business, financial condition and results of operations.

We rely on a network of independent dealers for the joint marketing of our products to small and mid-sized accounts, and to assist us in the marketing of our products to large accounts. We also rely upon these dealers to

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provide a variety of important specification, installation and after-market services to our clients. Our dealers operate, generally, under one-year, non-exclusive agreements. There is nothing to prevent our dealers from terminating their relationships with us. In addition, individual dealers may not continue to be viable and profitable. If dealers go out of business or are restructured, we may suffer losses because they may not be able to pay us for furniture previously delivered to them. The loss of a dealer relationship could also negatively affect our ability to maintain market share in the affected geographic market and to compete for and service clients in that market until a new dealer relationship is established. The loss or termination of a significant number of dealer relationships could cause significant difficulties for us in marketing and distributing our products, resulting in a decline in our sales.

One of our largest clients currently is the U.S. government, a relationship, which is subject to uncertain future funding levels and federal procurement laws and requires restrictive contract terms; any of these factors could curtail current or future business.

For the year ended December 31, 2006, we derived approximately 12.6% of our revenue from sales to various agencies and departments within the U.S. government. Our ability to compete successfully for and retain business with the U.S. government is highly dependent on cost-effective performance. Until recently, federal procurement laws required government agencies to purchase furniture products from Federal Prison Industries, Incorporated. If these or similar laws would be re-instituted, it would make it more difficult for us to sell our furniture to agencies and departments of the U.S. government. Our government business is also sensitive to changes in national and international priorities and U.S. government budgets.

The U.S. government typically can terminate or modify any of its contracts with us either for its convenience or if we default by failing to perform under the terms of the applicable contract. A termination arising out of our default could expose us to liability and impede our ability to compete in the future for contracts and orders. Furthermore, if we were found to have committed fraud or certain criminal offenses, we could be suspended or debarred from all further government contracting.

We operate with leverage, and a significant amount of cash will be required to service our indebtedness. Restrictions imposed by the terms of our indebtedness may limit our operating and financial flexibility.

As of December 31, 2006, we had total consolidated outstanding debt of approximately $350.3 million, which consisted of $254.7 million under our term loan facility, $95.0 million under our revolving credit facility and $0.6 million under local credit facilities maintained by our foreign subsidiaries. We also had $3.9 million outstanding commitments under letters of credit.

The terms of our credit facility permitted us to expand our revolving credit facility by an additional $12.0 million and our term loan facility by an additional $100.0 million, subject to certain limitations and satisfaction of certain conditions, including compliance with certain financial covenants.

As of December 31, 2006, the total remaining credit available to us under our credit facility and those of our foreign subsidiaries was $121.7 million. If we were to borrow the maximum available to us under our credit facility and those of our foreign subsidiaries, we would have total consolidated outstanding debt of approximately $472.0 million. The high level of our indebtedness could have important consequences to holders of our common stock, given that:

- a substantial portion of our cash flow from operations must be dedicated to fund scheduled payments of principal and debt service and will not be available for other purposes;
- our ability to obtain additional debt financing in the future for working capital, capital expenditures, research and development or acquisitions may be limited by the terms of our credit facility; and
- the terms of our credit facility also impose other operating and financial restrictions on us, which could limit our flexibility in reacting to changes in our industry or in economic conditions generally.

Our credit facility prevents us from incurring any additional indebtedness other than (i) borrowings under our existing credit facility; (ii) certain types of indebtedness that may be incurred subject to aggregate dollar limitations identified in the credit facility, including, without limitation, purchase money indebtedness and capital lease obligations not to exceed $30.0 million in the aggregate and unsecured indebtedness not to exceed $50.0 million in the aggregate, and (iii) other types of indebtedness that are not limited to specific dollar limitations, such as indebtedness incurred in the ordinary course of business and unsecured, subordinated indebtedness. The aggregate amount of indebtedness that we may incur pursuant to these exceptions is further limited by the financial covenants in our credit facility and, therefore, will depend on our future results of operations and cannot be determined at this time. Furthermore, although we may incur unlimited amounts of certain types of indebtedness, subject to compliance with these financial covenants, the amount of indebtedness that we may actually be able to incur will depend on the terms on which such types of debt financing are available to us, if available at all.

As a result of the foregoing, we may be prevented from engaging in transactions that might further our growth strategy or otherwise be considered beneficial to us. A breach of any of the covenants in our credit facility could result in a default thereunder. If payments to the lenders under our credit facility were to be accelerated, our assets could be insufficient to repay in full the indebtedness under our credit facility and our other liabilities. Any such acceleration could also result in a foreclosure on all or substantially all of our subsidiaries assets, which would have a negative impact on the value of our common stock and jeopardize our ability to continue as a going concern.

We may require additional capital in the future, which may not be available or may be available only on unfavorable terms.

Our capital requirements depend on many factors, including capital improvements, tooling and new product development. To the extent that our existing capital is insufficient to meet these requirements and cover any losses, we may need to raise additional funds through financings or curtail our growth and reduce our assets. Any equity or debt financing, if available at all, may be on terms that are not favorable to us. Equity financings could result in dilution to our stockholders, and the securities may have rights, preferences and privileges that are senior to those of our common stock. If our need for capital arises because of significant losses, the occurrence of these losses may make it more difficult for us to raise the necessary capital.

An inability to protect our intellectual property could have a significant impact on our business.

We attempt to protect our intellectual property rights, both in the United States and in foreign countries, through a combination of patent, trademark, copyright and trade secret laws, as well as licensing agreements and third-party nondisclosure and assignment agreements. Because of the differences in foreign trademark, patent and other laws concerning proprietary rights, our intellectual property rights do not generally receive the same degree of protection in foreign countries as they do in the United States. In some parts of the world, we have limited protections, if any, for our intellectual property. Our ability to compete effectively with our competitors depends, to a significant extent, on our ability to maintain the proprietary nature of our intellectual property. The degree of protection offered by the claims of the various patents, trademarks and service marks may not be broad enough to provide significant proprietary protection or competitive advantages to us, and patents, trademarks or service marks may not be issued on our pending or contemplated applications. In addition, not all of our products are covered by patents. It is also possible that our patents, trademarks and service marks may be challenged, invalidated, cancelled, narrowed or circumvented.

In the past, certain of our products have been copied and sold by others. We try to enforce our intellectual property rights, but we have to make choices about where and how we pursue enforcement and where we seek and maintain patent protection. In many cases, the cost of enforcing our rights is substantial, and we may determine that the costs of enforcement outweigh the potential benefits. If we are unable to maintain the proprietary nature of our intellectual property with respect to our significant current or proposed products, our competitors may be able to sell copies of our products, which could adversely affect our ability to sell our original products and could also result in competitive pricing pressures, which may negatively affect or profitability.

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If third parties claim that we infringe upon their intellectual property rights, we may incur liability and costs and may have to redesign or discontinue an infringing product.

We face the risk of claims that we have infringed third parties intellectual property rights. Companies operating in our industry routinely seek patent protection for their product designs, and many of our principal competitors have large patent portfolios. Prior to launching major new products in our key markets, we normally evaluate existing intellectual property rights. However, our competitors may have filed for patent protection which is not, at the time of our evaluation, a matter of public knowledge. Our efforts to identify and avoid infringing third parties intellectual property rights may not be successful. Any claims of patent or other intellectual property infringement, even those without merit, could (i) be expensive and time consuming to defend; (ii) cause us to cease making, licensing or using products that incorporate the challenged intellectual property; (iii) require us to redesign, reengineer, or rebrand our products or packaging, if feasible; or (iv) require us to enter into royalty or licensing agreements in order to obtain the right to use a third party s intellectual property.

We could be required to incur substantial costs to comply with environmental requirements. Violations of, and liabilities under, environmental laws and regulations may increase our costs or require us to change our business practices.

Our past and present ownership and operation of manufacturing plants are subject to extensive and changing federal, state, local and foreign environmental laws and regulations, including those relating to discharges to air, water and land, the handling and disposal of solid and hazardous waste and the cleanup of properties affected by hazardous substances. As a result, we are involved from time to time in administrative and judicial proceedings and inquiries relating to environmental matters and could become subject to fines or penalties related thereto. We cannot predict what environmental legislation or regulations will be enacted in the future, how existing or future laws or regulations will be administered or interpreted or what environmental conditions may be found to exist. Compliance with more stringent laws or regulations, or stricter interpretation of existing laws, may require additional expenditures by us, some of which may be material. We have been identified as a potentially responsible party pursuant to CERCLA for remediation costs associated with waste disposal sites previously used by us. In general, CERCLA can impose liability for costs to investigate and remediate contamination without regard to fault or the legality of disposal and, under certain circumstances, liability may be joint and several, resulting in one party being held responsible for the entire obligation. Liability may also include damages for harm to natural resources. The remediation costs and our allocated share at some of these CERCLA sites are unknown. We may also be subject to claims for personal injury or contribution relating to CERCLA sites. We reserve amounts for such matters when expenditures are probable and reasonably estimable.

We are subject to potential labor disruptions, which could have a significant impact on our business.

Certain of our employees located in Grand Rapids, Michigan and Italy are represented by unions. The collective bargaining agreement for our Grand Rapids location had an initial term effective through August 27, 2006. On August 25, 2006, we entered into a new five-year collective bargaining agreement with the Union covering bargaining unit members at the Grand Rapids, Michigan facility. The new collective bargaining agreement took effect on August 27, 2006. We have also had sporadic, to date unsuccessful, attempts to unionize our other North American manufacturing locations and have experienced a number of brief work stoppages at our facilities in Italy as a result of national and local issues. While we believe that we have good relations with our workforce, we may experience work stoppages or other labor problems in the future, and further unionization efforts may be successful. Any prolonged work stoppage could have an adverse effect on our reputation, our vendor relations and our dealership network. Moreover, because substantially all of our products are manufactured to order, we do not carry finished goods inventory that could mitigate the effects of a prolonged work stoppage.

Our insurance may not adequately insulate us from expenses for product defects.

We maintain product liability and other insurance coverage that we believe to be generally in accordance with industry practices, but our insurance coverage does not extend to field visits to repair, retrofit or replace defective products, or to product recalls. As a result, our insurance coverage may not be adequate to protect us fully against substantial claims and costs that may arise from product defects, particularly if we have a large number of defective products that we must repair, retrofit, replace or recall.

We may be vulnerable to the effects of currency exchange rate fluctuations, which could increase our expenses.

We primarily sell our products and report our financial results in U.S. dollars, but we generate some of our revenues and pay some of our expenses in other currencies. Paying our expenses in other currencies can result in a significant increase or decrease in the amount of those expenses in U.S. dollar terms, which affects our profits.

In the future, any foreign currency appreciation relative to the U.S. dollar would increase our expenses that are denominated in that currency. Additionally, as we report currency in the U.S. dollar, our financial position is affected by the strength of the currencies in countries where we have operations relative to the strength of the U.S. dollar. The principal foreign currencies in which we conduct business are the Canadian dollar and the Euro. Approximately 11.3% of our revenues in 2006 and 36.7% of our cost of goods sold in 2006 were denominated in currencies other than the U.S. dollar. From time to time we review our foreign currency exposure and evaluate whether we should enter into hedging transactions.

Risks Related to Our Common Stock

Our corporate documents and Delaware law contain provisions that could discourage, delay or prevent a change in control of our company.

Provisions in our amended and restated certificate of incorporation and bylaws may discourage, delay or prevent a merger or acquisition involving us that our stockholders may consider favorable. For example, our amended and restated certificate of incorporation authorizes our board of directors to issue up to 10,000,000 shares of blank check preferred stock. Without stockholder approval, the board of directors has the authority to attach special rights, including voting and dividend rights, to this preferred stock. With these rights, preferred stockholders could make it more difficult for a third party to acquire us. In addition, our amended and restated certificate of incorporation provides for a staggered board of directors, whereby directors serve for three-year terms, with approximately one third of the directors coming up for reelection each year. Having a staggered board will make it more difficult for a third party to obtain control of our board of directors through a proxy contest, which may be a necessary step in an acquisition of us that is not favored by our board of directors.

We are also subject to the anti-takeover provisions of Section 203 of the Delaware General Corporation Law. Under these provisions, if anyone becomes an interested stockholder, we may not enter into a business combination with that person for three years without special approval, which could discourage a third party from making a takeover offer and could delay or prevent a change of control. For purposes of Section 203, interested stockholder means, generally, someone owning 15% or more of our outstanding voting stock or an affiliate of ours that owned 15% or more of our outstanding voting stock during the past three years, subject to certain exceptions as described in Section 203. Upon any change in control, the lenders under our credit facility would have the right to require us to repay all of our outstanding obligations under the facility.

Our stock price may be volatile, and your investment in our common stock could suffer a decline in value.

There has been significant volatility in the market price and trading volume of equity securities, which may be unrelated to the financial performance of the companies issuing the securities. These broad market fluctuations may negatively affect the market price of our common stock. You may not be able to resell your shares at or above the price at which you purchased them due to fluctuations in the market price of our common stock caused by changes in our operating performance or prospects and other factors. Some specific factors that may have a significant effect on our common stock market price include:

- actual or anticipated fluctuations in our operating results or future prospects;

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our announcements or our competitors announcements of new products;

the public s reaction to our press releases, our other public announcements and our filings with the SEC;

strategic actions by us or our competitors, such as acquisitions or restructurings;

new laws or regulations or new interpretations of existing laws or regulations applicable to our business;

changes in accounting standards, policies, guidance, interpretations or principles;

changes in our growth rates or our competitors growth rates;

our inability to raise additional capital;

conditions of the office furniture industry as a result of changes in financial markets or general economic conditions, including those resulting from war, incidents of terrorism and responses to such events;

sales of common stock by us or members of our management team; and

changes in stock market analyst recommendations or earnings estimates regarding our common stock, other comparable companies or the office furniture industry generally.

Item 1B. ***Unresolved Staff Comments***

None

Item 2. ***Properties***

We operate over 2,837,000 square feet of facilities, including manufacturing plants, warehouses and sales offices. Of these facilities, we own approximately 2,236,000 square feet and lease approximately 601,000 square feet. Our manufacturing plants are located in East Greenville, Pennsylvania, Grand Rapids and Muskegon, Michigan, Toronto, Canada, and Foligno and Graffignana, Italy. The location, square footage, and use of the facilities as of December 31, 2006 are shown below.

Owned Locations	Square Footage	Use
East Greenville, Pennsylvania	547,000 (1)	Corporate Headquarters, Manufacturing, Warehouses, and Administration
Grand Rapids, Michigan	545,000 (1)	Manufacturing and Administration
Muskegon, Michigan	368,000 (1)	Manufacturing and Administration
Toronto, Canada	408,000	Manufacturing, Distribution, Warehouses, and Administration
Foligno, Italy	258,000	Manufacturing, Distribution, Warehouses, and Administration
Graffignana, Italy	110,000	Manufacturing, Distribution, Warehouses, and Administration

Leased Locations	Square Footage	Use
East Greenville, Pennsylvania	142,000 (2)	Warehouses, Distribution
Muskegon, Michigan	105,000	Manufacturing
Toronto, Canada	79,000	Manufacturing
Knoll, Europe	42,000	Administration, Warehouses

(1) Facilities are encumbered by mortgages securing indebtedness under our senior credit agreement.

(2) These are three warehouses that have been subleased to a third party logistics provider and serve as our northeast distribution center.

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We believe that our plants and other facilities are sufficient for our needs for the foreseeable future.

Item 3. ***Legal Proceedings***

From time to time we are subject to litigation or other legal proceedings arising in the ordinary course of business. Based upon information currently known to us, we believe the outcome of such proceedings will not have, individually or in the aggregate, a material adverse effect on our business, financial condition or results of operations.

Chicago Transit Authority Project

On May 15, 2006, we received a federal grand jury subpoena from the U.S. Attorneys Office in Chicago requesting that we produce certain documents associated with the sale in 2003 and 2004 of furniture for use in the Chicago Transit Authority s new headquarters in Chicago. We were one of a number of companies that provided goods or services in connection with the project. We are cooperating with the investigation by the U.S. Attorneys Office.

Item 4. ***Submission of Matters To A Vote of Security Holders***

No matters were submitted to a vote of security holders in the fourth quarter of 2006.

PART II

Item 5. ***Market for Registrant s Common Equity, Related Shareholder Matters And Issuer Purchases of Equity Securities***

Market Information and Dividend Policy

Our common stock has been listed on the New York Stock Exchange (NYSE) since December 14, 2004, the date of our initial public offering, under the symbol KNL. As of March 9, 2007, there were approximately 42 stockholders of record of our common stock.

The following table sets forth, for the periods indicated, high and low closing sales prices for the common stock as reported by the NYSE.

	High	Low
Fiscal year ended December 31, 2006		
First quarter	$ 21.44	$ 16.43
Second quarter	$ 22.43	$ 18.12
Third quarter	$ 20.30	$ 16.90
Fourth quarter	$ 22.15	$ 19.34
Fiscal year ended December 31, 2005		
First quarter	$ 17.75	$ 16.20
Second quarter	$ 17.47	$ 16.17
Third quarter	$ 18.90	$ 17.14
Fourth quarter	$ 18.25	$ 14.95

We declared and paid cash dividends of $0.25 per share and $0.41 per share during the years ended December 31, 2005 and 2006, respectively. Our board of directors currently intends to declare and pay quarterly dividends of $0.11 per share on our common stock. The declaration and payment of dividends is subject to the discretion of our board of directors and depends on various factors, including our net income, financial condition, cash requirements and future prospects and other factors deemed relevant by our board of directors. Our credit

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facility imposes restrictions on our ability to pay dividends, and thus our ability to pay dividends on our common stock will depend upon, among other things, our level of indebtedness at the time of the proposed dividend and whether we are in default under any of our debt obligations. Our future dividend policy will also depend on the requirements of any future financing agreements to which we may be a party.

Performance Graph

The following line graph compares the cumulative total stockholder return on our common stock with the cumulative total return of the Standard & Poors 500 Stock Index and with the cumulative total return on a peer group of companies selected by us for the period commencing on December 14, 2004, the date our shares began trading publicly, and ending on December 31, 2006. Our share price at the beginning of the measurement period is $15.00 per share, the price in our initial public offering. The graph and table assume that $100 was invested on December 14, 2004 in each of Knoll common stock and the stock of our peer group, and on November 30, 2004 in the S&P 500 Index, and that all dividends were reinvested. Cumulative total stockholder returns for Knoll common stock, the S&P 500 Index, and the stock of our peer group are based on Knoll s fiscal year. Our peer group is made up of two publicly-held manufacturers of office furniture, Herman Miller, Inc. and Steelcase, Inc. The stock performance on the graph below does not necessarily indicate future price performance.

	12/14/04	12/04	12/05	12/06
Knoll, Inc.	**100.00**	**116.67**	**115.69**	**151.92**
S & P 500	**100.00**	**103.40**	**108.48**	**125.62**
Peer Group	**100.00**	**109.18**	**117.06**	**147.37**

Repurchases of Equity Securities

The following is a summary of share repurchase activity during the three months ended December 31, 2006.

On August 17, 2005, our board of directors approved a stock repurchase program (the Options Proceeds Program), whereby they authorized us to purchase shares of our common stock in the open market using the cash proceeds received by us upon exercise of outstanding options.

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On February 2, 2006, our board of directors approved an additional stock repurchase program, pursuant to which we are authorized to purchase up to $50.0 million of our common stock in the open market, through privately negotiated transactions, or otherwise. .

In addition, from time-to-time, we repurchase shares of common stock under our 401(k) retirement savings plan. In 1999, we issued shares of common stock to the accounts of all actively employed U.S. participants under our 401(k) retirement savings plan. Upon retirement, death, or termination of employment, these participants may sell vested shares of common stock back to us. When a participant elects to sell vested shares back to us, we may elect to purchase those shares or cause them to be sold in the open market.

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as part of publicly Announced Plans or Programs (2)	Maximum Dollar Value of Shares that may yet be Purchased Under the Plans or Programs (2)
October 1, 2006 - October 31, 2006	69,907	20.36	69,607 (3)	36,720,679
November 1, 2006 - November 30, 2006	266,790	20.23	265,890 (4)	34,821,944
December 1, 2006 - December 31, 2006	79,756	21.31	79,756 (5)	34,821,944
Total	416,453		415,253	

(1) 1,200 of these shares were purchased under our 401(k) retirement savings plan.

(2) There is no limit on the number or value of shares that may be purchased by us under the Options Proceeds Program. Under our $50.0 million stock repurchase program we are only authorized to spend an aggregate of $50.0 million on stock repurchases. There is no scheduled expiration date for the Option Proceeds Program or the $50.0 million stock repurchase program, but our board of directors may terminate either program in the future.

(3) These shares were purchased under the Option Proceeds Program . Our Options Proceeds Program was publicly announced on August 17, 2005 and our $50.0 million stock repurchase program was publicly announced on February 3, 2006.

(4) 168,590 of these shares were purchased under the Options Proceeds Program and 97,300 of these shares were purchased under our $50.0 million stock repurchase program approved by our board of directors on February 2, 2006.

(5) These shares were purchased under the Options Proceeds Program.

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Item 6. ***Selected Consolidated Financial Data***

The following selected consolidated financial data should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes included elsewhere in this Form 10-K. The selected consolidated financial data for the years ended December 31, 2004, 2005 and 2006 and as of December 31, 2005 and 2006 are derived from our audited financial statements included elsewhere in this Form 10-K. The selected consolidated financial data for the years ended December 31, 2002 and 2003 and as of December 31, 2002, 2003 and 2004 are derived from our audited financial statements not included in this Form 10-K (in thousands, except per share data).

	Years Ended December 31,				
	2002	2003	2004	2005	2006
	(dollars in thousands, except shares and per share data)				
Consolidated Statement of Operations Data:					
Sales	$ 773,263	$ 697,246	$ 706,390	$ 807,960	$ 982,152
Cost of sales	492,902	460,911	465,379	535,904	663,115
Gross profit	280,361	236,335	241,011	272,056	319,037
Selling, general and administrative expenses	156,314	149,739	169,706	179,217	202,097
Operating income	124,047	86,596	71,305	92,839	116,940
Interest Expense	26,541	20,229	19,452	23,684	23,717
Other income (expense), net	2,933	(2,473)	(5,316)	(5,355)	741
Income before income tax expense	100,439	63,894	46,537	63,800	93,964
Income tax expense	40,667	27,545	19,793	27,891	35,331
Net income	$ 59,772	$ 36,349	$ 26,744	$ 35,909	$ 58,633
Per Share Data:					
Earnings per share:					
Basic	$ 1.29	$ 0.78	$ 0.58	$ 0.70	$ 1.18
Diluted	$ 1.23	$ 0.75	$ 0.55	$ 0.68	$ 1.14
Cash dividends declared per share:	$	$	$ 1.525	$ 0.25	$ 0.41
Weighted average shares outstanding					
Basic	46,345,714	46,317,530	46,353,253	51,219,123	49,606,677
Diluted	48,474,648	48,414,374	48,319,483	52,919,388	51,238,088

	As of December 31,				
	2002	2003	2004	2005	2006
	(in thousands)				
Consolidated Balance Sheet Data:					
Working (deficit) capital	$ (14,419)	$ (28,238)	$ 67,492	$ 63,993	$ 77,170
Total assets	590,351	561,001	574,239	582,546	632,137
Total long-term debt, including current portion	452,042	380,871	392,858	316,038	350,316
Total liabilities	653,474	569,120	595,584	544,830	627,753
Stockholders (deficit) equity	(63,123)	(8,119)	(21,345)	37,716	4,384

Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

Management s discussion and analysis of financial condition and results of operations provides an account of our financial performance and financial condition that should be read in conjunction with the accompanying consolidated financial statements.

Overview

The fourth quarter of 2006 ended a very positive year for Knoll. This year we were able to further expand our industry leading margins and deliver very strong double digit growth in sales, operating profit, net income and earnings per share. This is the second consecutive year in which we delivered double digit growth better than the industry. Net sales for the year were $982.2 million, an increase of 21.6% over 2005. Operating income and net income were $116.9 million and $58.6 million, an increase of 26.0% and 63.2%, respectively, over the full year 2005. Earnings per share rose from $0.70 in 2005 to $1.18 in 2006, an increase of 68.6%.

Over the past several years we have been working to increase our share in non-systems categories by cross selling to our office systems clients and securing stand-alone opportunities for the sales of seating, files and storage, and casegoods. We have actively expanded our product lines in these non-systems categories to help us pursue a larger share of the U.S. market for those goods. In 2002, we introduced the award winning and commercially successful *LIFE* chair to drive our growth in the seating category and compete in the high-performance work chair market. In 2004, we introduced the *Knoll Essentials* collection of easy-to-order, best-selling products from our broad range of office furnishings and quadrupled our storage offering. During 2005, we increased the pace of our new product introductions for our *Knoll Textiles* collection of upholstery, panel fabrics, wall coverings and drapery and continued to expand our retail distribution network for our *KnollStudio* collection of chairs, barstools, lounge seating, conference, dining and occasional tables to take advantage of increased consumer interest in modern and mid-century design, showcase our design strength and broaden recognition of the Knoll brand. We introduced our *Chadwick* chair in 2005 and introduced our *Essentials* chair collection in January 2006.

In 2006, we were able to gain share in the systems area because of our broad offerings. We also continued to gain marketing share in our seating, storage, and specialty products. Our *Knoll Essentials* dealer marketing program set another record with over 50% shipment growth and our high margin specialty businesses delivered record breaking sales as we expanded our marketing efforts in the retail, consumer and international spaces.

During 2006, our gross margins declined to 32.5% from 33.7% a year ago. This decline is the result of several factors including a shift in the mix of products sold due to increased systems growth, continued inflationary pressures in raw materials and transportation, inefficiencies in our manufacturing operations caused by the higher demand and additional transportation costs incurred as a result of expediting shipments to customers and for in bound shipments. Higher material, labor, and transportation costs negatively impacted 2006 gross profit by approximately $20.3 million. These costs were partially offset by price realization, global sourcing and continuous improvement efforts. In addition, the appreciation of the Canadian dollar had the effect of decreasing 2006 gross profit by approximately $7.1 million due to higher product costs compared to 2005. Factory efficiencies are improving with our expanded production and we are seeing the benefit of fixed cost absorption from higher sales. We improved our manufacturing capacity by adding more shifts and investing in additional machinery.

For the year we were able to improve our leverage ratio, reduce our share count and increase our dividend as we put our free cash flow and strengthened balance sheet to work for the benefit of our shareholders. We increased our fourth quarter dividend by 10% over the prior three quarters. In addition, we became a fully independent public company with the combination of the completion of our August secondary stock offering, a stock purchase from Warburg Pincus Ventures, L.P. of 3.9 million shares, and the private distribution by Warburg Pincus of its remaining shares. Warburg Pincus no longer holds an equity interest in Knoll. In connection with the Warburg buyback and our stock repurchase programs we repurchased approximately 6.0 million shares during 2006. The cash flow to repurchase these shares was generated from operations and net borrowings of $34.2 million. In addition, we spent $13.4 million on capital expenditures as compared to $10.7 million for 2005. Investing activities in 2006 also included $3.3 million paid for intangibles related to investments in our seating line.

Overall our strong performance in 2006 enhanced our ability to invest in initiatives that drive top-line growth, improve margins, and increase shareholder value.

Critical Accounting Policies

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of certain assets, liabilities, revenues and expenses and the disclosure of certain contingent assets and liabilities. Actual results may differ from such estimates. We believe that the critical accounting policies that follow are those policies that require the most judgment, estimation and assumption in preparing our consolidated financial statements.

Allowance for Doubtful Accounts

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our clients and dealers to make required payments. The allowance is determined through an analysis of the aging of accounts receivable and assessments of risk that are based on historical trends and an evaluation of the impact of current and projected economic conditions. We evaluate the past-due status of our trade receivables based on contractual terms of sale. If the financial condition of our clients and dealers were to deteriorate, additional allowances may be required. Accounts receivable are charged off against the allowance for doubtful accounts when we determine that recovery is unlikely.

Inventory

Inventories are valued at the lower of cost or market. Cost is determined using the first-in, first-out method. We write down inventory that, in our judgment, is impaired or obsolete. Obsolescence may be caused by the discontinuance of a product line, changes in product material specifications, replacement products in the marketplace and other competitive influences.

Goodwill and Other Intangible Assets

Intangible assets consist of goodwill, trademarks and deferred financing fees. Goodwill is recorded at the amount by which cost exceeds the net assets of acquired businesses, and all other intangible assets are recorded at cost. Goodwill and other intangible assets are tested for impairment at least annually rather than being amortized.

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On December 19, 2006, we purchased certain intangibles as an investment in its seating line. A definite useful life was assigned to these intangibles and as such amortization will be recorded over the economic life of the intangibles in accordance with Statement of Financial Accounting Standards 142 Goodwill and Other Intangible Assets .

Deferred financing costs that are incurred by us in connection with the issuance of debt are deferred and amortized to interest expense over the life of the underlying indebtedness

Product Warranty

We provide for the estimated cost of product warranties at the time revenue is recognized. While we engage in product quality programs and processes, our warranty obligation is affected by product failure rates and by material usage and service costs incurred in correcting a product failure. Cost estimates are based on historical product failure rates and identified one-time fixes for each specific product category. Warranty cost generally varies in direct relation to sales volume, as such costs tend to be a consistent percentage of revenue. Should actual costs differ from original estimates, revisions to the estimated warranty liability would be required.

Employee Benefits

We are partially self-insured for our employee health benefits. We accrue for employee health benefit obligations based on an actuarial valuation. The actuarial valuation is based upon historical claims as well as a number of assumptions, including rates of inflation for medical costs, and benefit plan changes. Actual results could be materially different from the estimates used.

Pension and Other Postretirement Benefits

We sponsor two defined benefit pension plans and two other postretirement benefit plans that cover substantially all our U.S. employees. Several statistical and other factors, which attempt to anticipate future events, are used in calculating the expense and liability related to the plans. Key factors include assumptions about the expected rates of return on plan assets, discount rates, and health care cost trend rates, as determined by us, within certain guidelines. We consider market conditions, including changes in investment returns and interest rates, in making these assumptions.

We determine the expected long-term rate of return on plan assets based on aggregating the expected rates of return for each component of the plan s asset mix. We use historic plan asset returns combined with current market conditions to estimate the rate of return. The expected rate of return on plan assets is a long-term assumption and generally does not change annually. The discount rate reflects the market rate for high-quality fixed income debt instruments as of our annual measurement date and is subject to change each year. Holding all other assumptions constant, a one-percentage-point increase or decrease in the assumed rate of return on plan assets would decrease or increase, respectively, 2006 net periodic pension expense by approximately $0.7 million. Likewise, a one percentage point increase or decrease in the discount rate would decrease or increase, respectively, 2006 net periodic pension expense by approximately $2.8 million or $3.9 million, respectively.

Unrecognized actuarial gains and losses are recognized over the expected remaining service life of the employee group. Unrecognized actuarial gains and losses arise from several factors, including experience and assumption changes with respect to the obligations and from the difference between expected returns and actual returns on plan assets. These unrecognized gain and losses are systematically recognized as a change in future net periodic pension expense in accordance with FASB Statement No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB No. 87, 88, 106, and 132(R)* (SFAS 158).

Key assumptions we use in determining the amount of the obligation and expense recorded for postretirement benefits other than pensions (OPEB), under FASB Statement No. 106, *Employers Accounting* *for Postretirement Benefits Other Than Pensions*, include the assumed discount rate and the assumed rate of increases in future health care costs. The discount rate we use to determine the obligation for these benefits matches the discount rate used in determining our pension obligations in each year presented. In estimating the health care cost trend rate, we consider actual health care cost experience, future benefit structures, industry trends and advice from our actuaries. We assume that the relative increase in health care costs will generally trend downward over the next several years, reflecting assumed increases in efficiency in the health care system and industry-wide cost containment initiatives. At December 31, 2006, the expected rate of increase in future health care costs was 9% in determining the benefit obligation for 2007 and 7% in determining the net periodic benefit cost for 2006. The rate was then assumed to decrease 1.0% per year to an ultimate rate of 5% for 2011 and thereafter for the benefit obligation. Increasing the assumed health care cost trend by one percentage point in each year would increase the benefit obligation as of December 31, 2006, by $4.2 million and increase the aggregate of the service and interest cost components of net periodic benefit cost for 2006 by approximately $0.3 million. Decreasing the assumed health care cost trend rate by one percentage point in each year would decrease the benefit obligation as of December 31, 2006 by approximately $3.4 million and decrease the aggregate of the service and interest cost components of net periodic benefit cost for 2006 by approximately $0.2 million.

In accordance with SFAS 158, we recognized in our statement of financial position the funded status (i.e. the difference between the fair value of plan assets and the projected benefit obligation) of our defined benefit pension and postretirement benefit plans. To record the unfunded status of our plans we recorded an additional liability and an adjustment to accumulated other comprehensive income, net of tax. For further information on how this new accounting pronouncement affects our financial results see note 14 in the accompanying financial statements.

The actuarial assumptions we use in determining our pension and OPEB retirement benefits may differ materially from actual results due to changing market and economic conditions, higher or lower withdrawal rates, or longer or shorter life spans of participants. While we believe that the assumptions used are appropriate, differences in actual experience or changes in assumptions may materially affect our financial position or results of operations.

Commitments and Contingencies

We establish reserves for the estimated cost of environmental and legal contingencies when such expenditures are probable and reasonably estimable. A significant amount of judgment and use of estimates is required to quantify our ultimate exposure in these matters. We engage outside experts as deemed necessary or appropriate to assist in the evaluation of exposure. From time to time, as information becomes available regarding changes in circumstances for ongoing issues as well as information regarding emerging issues, our potential liability is reassessed and reserve balances are adjusted as necessary. Revisions to our estimates of potential liability, and actual expenditures related to environmental and legal contingencies, could have a material impact on our results of operations or financial position.

Taxes

We account for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes*, (SFAS 109) which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between book and tax bases of recorded assets and liabilities. SFAS No. 109 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion or all of the deferred tax assets will not be recognized.

At December 31, 2006, deferred tax liabilities of $71.7 million exceeded deferred tax assets of $43.5 million by $28.2 million. At December 31, 2005, our deferred tax liabilities of $66.8 million exceeded our deferred tax assets of $31.9 million by $34.9 million.

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Our deferred tax assets at December 31, 2006 and 2005 of $43.5 million and $31.9 million, respectively, are net of valuation allowances of $17.9 million and $16.8 million, respectively. We have recorded the above valuation allowance primarily for net operating loss carryforwards in foreign tax jurisdictions where we have incurred historical tax losses from operations or acquired tax losses through acquisition, and have determined that it is more likely than not that these deferred tax assets will not be realized.

We evaluate on a quarterly basis the realizability of our deferred tax assets and adjust the amount of the allowance, if necessary. The factors used to assess the likelihood of realization include our forecast of future taxable income and our assessment of available tax planning strategies that could be implemented to realize the net deferred tax assets.

Interest Rate Swap and Cap Agreements

We account for our interest rate swap and cap agreements in accordance with Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended (SFAS 133). Our interest rate swap agreement, which matured on September 29, 2006, was classified as a cash flow hedge and, as such, the effective portion of the change in the value of the contract was recorded in other comprehensive income, net of tax, and reclassified into earnings in the period or periods during which the hedged transaction affects earnings. Our old interest rate cap agreement, which also matured on September 29, 2006, and our two new interest rate cap agreements entered into on September 30, 2006, are classified as risk management instruments and management has elected to not apply hedge accounting. As such, the change in fair value of the contracts is reported in earnings in the period the value of the contract changes as a component of other income (expense). Changes in valuation assumptions and estimates used by the counterparties could materially affect our results of operations or financial position.

Results of Operations

Years ended December 31, 2005 and 2006

	Three Months Ended				Twelve Months Ended	Three Months Ended				Twelve Months Ended
	March 31, 2005	June 30, 2005	September 30, 2005	December 31, 2005	December 31, 2005	March 31, 2006	June 30, 2006	September 30, 2006	December 31, 2006	December 31, 2006
					(unaudited)					
	(in thousands, except statistical data)									
Consolidated Statement of Operations Data:										
Sales	$ 179,129	$ 197,726	$ 209,333	$ 221,772	$ 807,960	$ 218,100	$ 247,476	$ 243,609	$ 272,967	$ 982,152
Gross profit	58,089	68,187	71,433	74,347	272,056	69,773	78,965	81,220	89,079	319,037
Operating income	17,019	24,095	26,323	25,402	92,839	21,937	29,236	30,158	35,609	116,940
Interest expense	6,087	6,000	6,214	5,383	23,684	5,347	5,449	5,983	6,938	23,717
Other income (expense), net	514	338	(1,933)	(4,274)	(5,355)	237	525	(309)	288	741
Income tax expense	4,595	7,065	9,980	6,251	27,891	6,574	9,560	8,227	10,970	35,331
Net income	$ 6,851	$ 11,368	$ 8,196	$ 9,494	$ 35,909	$ 10,253	$ 14,752	$ 15,639	$ 17,989	$ 58,633
Statistical and Other Data:										
Sales growth from comparable prior year	16.8%	10.6%	15.4%	15.0%	14.4%	21.8%	25.2%	16.4%	23.1%	21.6%
Gross profit margin	32.4%	34.5%	34.1%	33.5%	33.7%	32.0%	31.9%	33.3%	32.6%	32.5%
Backlog	$ 117,209	$ 131,234	$ 125,409	$ 147,289	$ 147,289	$ 173,826	$ 169,878	$ 170,609	$ 167,728	$ 167,728

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Sales

Sales for 2006 were $982.2 million, an increase of $174.2 million, or 21.6%, from sales of $808.0 million for 2005. The sales increase was primarily due to increased sales across all our product categories and Europe primarily as a result of continued growth recovery in the industry. For each quarter in 2006, we experienced a greater than 15% increase in sales over the comparable prior year period. Approximately $3.4 million of the increase for total year sales, or approximately 2%, was attributable to additional revenues realized from price increases. The highest growth rate was led by our seating and storage lines, and followed by our specialty product lines and systems. Systems, which hold our largest product category shares, increased 21% alone. At December 31, 2006, sales backlog was $167.7 million, an increase of $20.4 million, or 13.8%, from sales backlog of $147.3 million as of December 31, 2005.

Gross Profit and Operating Income

Gross profit for 2006 was $319.0 million, an increase of $46.9 million, or 17.2%, from gross profit of $272.1 million for 2005. Operating income for 2006 was $116.9 million, an increase of $24.1 million, or 26.0%, from operating income of $92.8 million for 2005.

As a percentage of sales, gross profit decreased from 33.7% for 2005 to 32.5% for 2006. Operating income as a percentage of sales increased from 11.5% to 11.9% over the same period. Gross profit for 2006 was negatively impacted by the appreciation of the Canadian dollar by approximately $7.1 million due to higher product costs in 2006 compared to 2005. Higher material, labor, and transportation costs also negatively impacted gross profit by approximately $23.5 million. We were able to partially offset these costs through price realization, continuous improvement and global sourcing initiatives.

Operating margins benefited from better absorption of overhead on incremental volume. Operating expenses for 2006 were $202.1 million, or 20.6% of sales, compared to $179.2 million, or 22.2% of sales, for 2005. Operating expenses in 2006 included approximately $1.2 million of costs related to our secondary public offerings completed in February and August 2006, $137 thousand of costs incurred in connection with our buyback of 3.9 million shares from Warburg Pincus and additional bank and related fees of $258 thousand due to the amendment of our credit facility. Operating expense in 2006 also increased as a result of higher selling expenses and sales and incentive compensation directly attributable to increase sales dollars.

Interest Expense

Interest expense for 2006 and 2005 was $23.7 million. The decrease in interest expense at the beginning of 2006 was largely due to lower average debt balances was offset by an increase in the third and fourth quarters with our debt expansion.

The weighted average rate for 2006 was approximately 7.2%. The weighted average rate for 2005 was approximately 6.4%.

Other Income (Expense), Net

Other income for 2006 was $0.7 million comprised primarily of a $0.6 million gain due to our foreign currency translation, a $0.7 million unrealized loss on our interest rate cap agreements, and $0.8 million in other miscellaneous income. Other expense for 2005 was $5.4 million comprised primarily of $2.3 million of foreign exchange transaction losses, a $3.6 million write off of deferred financing fees related to the amendment and restatement or our credit facility, and $1.0 million of costs incurred in putting the facility in place.

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Income Tax Expense

The mix of pretax income and the varying effective tax rates in the countries in which we operate directly affects our consolidated effective tax rate. The effective tax rate was 37.6% for 2006 compared to 43.7 % for 2005. Tax expense in 2005 included $3.1 million of taxes related to the one-time repatriation of $45 million of Canadian earnings under The American Job Creations Act.

Years ended December 31, 2004 and 2005

Sales

Sales for 2005 were $808.0 million, an increase of $101.6 million, or 14.4%, from sales of $706.4 million for 2004. The sales increase was primarily due to increased sales across all our product categories and Europe primarily as a result improved conditions in the industry. For each quarter in 2005, we experienced a greater than 10% increase in sales over the comparable prior year period, and the quarter ending December 31, 2005 marked the seventh consecutive quarter of year-over-year growth. Price realization, resulting from price increases implemented during 2004 and adjustments to product discounts, contributed $13.4 million during 2005.

At December 31, 2005, sales backlog was $147.3 million, an increase of $24.8 million, or 20.2%, from sales backlog of $122.5 million as of December 31, 2004.

Gross Profit and Operating Income

Gross profit for 2005 was $272.1 million, an increase of $31.1 million, or 12.9%, from gross profit of $241.0 million for 2004. Operating income for 2005 was $92.8 million, an increase of $21.5 million, or 30.2%, from operating income of $71.3 million for 2004.

As a percentage of sales, gross profit decreased from 34.1% for 2004 to 33.7% for 2005. Operating income as a percentage of sales increased from 10.1% to 11.5% over the same period. Gross profit for 2005 includes $0.8 million of restructuring charges related to the exiting of one our leased facilities in Canada concurrent with the expiration of the lease. The appreciation of the Canadian dollar also had the effect of decreasing gross profit by approximately $5.5 million due to higher product costs in 2005 compared to 2004. We were able to offset increased material and transportation costs of $21.2 million through $13.4 million of price realization, and $8.1 million of continuous improvement and global sourcing initiatives. Without the appreciation of the Canadian dollar and the additional restructuring charges, gross profit margin for 2005 would have remained substantially consistent with the prior year.

Operating margins benefited from better absorption of overhead on incremental volume. Operating expenses for 2005 were $179.2 million, or 22.2% of sales, compared to $169.7 million, or 24.0% of sales for 2004. Operating expense in 2005 included approximately $4.0 million of stock-based compensation, $3.1 million of costs of operating as a public company and higher sales compensation due to strong bookings during the year of approximately $4.5 million. Operating expense in 2004 included $4.4 million of costs associated with our initial public offering.

Interest Expense

Interest expense for 2005 was $23.7 million, an increase of $4.2 million from 2004. The increase in interest expense was largely due to higher interest rates that were in effect under our old credit facility which was in place through September 30, 2005. On October 3, 2005, we amended and restated our existing facility for a new facility which provides for lower rates.

The weighted average rate for 2005 was approximately 6.4%. The weighted average rate for 2004 was approximately 4.3%.

Other Income (Expense), Net

Other expense for 2005 was $5.4 million comprised primarily of $2.3 million of foreign exchange transaction losses, a $3.6 million write off of deferred financing fees related to the amendment and restatement or our credit facility, and $1.0 million of costs incurred in putting the facility in place. Other expense for December 31, 2004 was $5.3 million comprised primarily of $3.4 million of foreign exchange transaction losses and a $2.5 million write off deferred financing fees due to the refinancing of our credit facility in 2004.

Income Tax Expense

The mix of pretax income and the varying effective tax rates in the countries in which we operate directly affects our consolidated effective tax rate. The effective tax rate was 43.7% for 2005 compared to 42.5 % for 2004. Tax expense in 2005 included $3.1 million of taxes related to the one-time repatriation of $45 million of Canadian earnings under The American Job Creations Act. Tax expense in 2004 included $2.9 million of non-deductible costs associated with our initial public offering as well as non U.S. tax losses for which a benefit was not recorded. Both of these items increased the 2004 effective tax rate over the anticipated statutory rates.

Liquidity and Capital Resources

The following table highlights certain key cash flows and capital information pertinent to the discussion that follows:

	2006	2005	2004
		(in thousands)	
Cash provided by operating activities	$ 77,528	$ 77,441	$ 60,303
Capital expenditures	13,362	10,744	13,131
Net cash used in investing activities	16,578	10,643	13,131
Purchase of common stock	107,799	3,065	220
Net proceeds from (repayment of) debt	34,173	(76,723)	11,896
Payment of dividends	20,195	12,490	70,601
Net proceeds from issuance of stock	27,249	31,390	13,216
Net cash used for financing activities	56,414	64,159	51,528

Historically, we have carried significant amounts of debt, and cash generated by operating activities has been used to fund working capital, capital expenditures and scheduled payments of principal and interest under our debt. Our capital expenditures are typically for new product tooling and manufacturing equipment. These capital expenditures support new products and continuous improvements in our manufacturing processes. Beginning during the second quarter of 2006, we implemented our $50.0 million discretionary stock repurchase program and began using cash generated by operating activities to buy back shares.

We use our revolving credit facility in the ordinary course of business to fund our working capital needs, and at times make significant borrowings and repayments under the revolving facility depending on our cash needs and availability at such time.

In addition, on August 8, 2006, we purchased 3,900,000 shares of common stock from Warburg, Pincus Ventures, L.P. in a private non-underwritten transaction at a price of $16.9095 per share. In connection with this purchase, we increased our revolving credit facility by $12 million and increased our term loan facility by $38 million, pursuant to an accordion feature in our credit facility. We then borrowed approximately $66 million to finance the above-referenced purchase of shares from Warburg, Pincus Ventures, L.P.

The stock purchase from Warburg, Pincus Ventures, L.P. was not part of our $50 million stock repurchase program and did not count towards the $50.0 million limit under that repurchase program. As of December 31,

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2006, we purchased approximately $15.2 million in Knoll common stock under the $50 million stock repurchase program. The stock purchase from Warburg, Pincus Ventures, L.P. was also not part of our stock repurchase plan that uses the proceeds of stock option exercises to repurchase outstanding shares. For the year ended December 31, 2006, we purchased 1,330,456 shares for approximately $26.5 million under the option proceeds program.

Net cash provided by operating activities was $77.5 million in 2006, $77.4 million in 2005 and $60.3 million in 2004. The increase in operating cash flow in 2006 was largely a result of an increase of $22.7 million in net income. This increase was offset with increased spending to fund our working capital as a result of higher sales volumes. In addition, with the implementation of FAS 123 (R), the tax benefit from stock options is now included in financing activities as a cash inflow rather than in operating activities as it was in 2005. The increase in operating cash flow in 2005 was largely a result of an increase of $9.2 million in net income and a $2.9 million increase in the tax benefit from the exercise of stock options and a $3.9 increase in non-cash earned stock grant compensation.

For the year ended December 31, 2006, we used available cash, including the $77.5 million of net cash from operating activities, $27.2 million of proceeds from the issuance of common stock, and $34.2 million of net borrowings, to fund $13.4 million in capital expenditures, purchase $3.3 million of intangibles, repurchase $107.8 million of common stock for treasury, fund dividend payments to shareholders totaling $20.2 million, and fund working capital. The 3.9 million shares purchased from Warburg, Pincus Ventures, L.P. in August is included in the $107.8 million of common stock repurchased for treasury. In 2005, we used available cash, including the $77.4 million of net cash provided from operations, $316.0 million of proceeds from our new credit facility, and $31.4 million of proceeds from the issuance of common stock, to fund $10.7 million of capital expenditures, repay $392.7 million of debt, and fund dividend payments to shareholders totaling $12.5 million. In 2004, we used available cash, including the $60.3 million of net cash from operations, $425.0 million of proceeds from our credit facility, and $13.2 million of proceeds from the issuance of stock to fund $13.1 million in capital expenditures, repay $413.1 of existing debt, and fund a dividend payment to shareholders totaling $70.6 million.

Cash used in investing activities was $16.6 million in 2006, $10.6 million in 2005 and $13.1 million in 2004. Fluctuations in cash used in investing activities are primarily attributable to the levels of capital expenditures. In 2006, we invested $3.3 million for the purchase of intangibles related to our seating line. We estimate that our capital expenditures in 2007 will be approximately $22 million.

On October 3, 2005, we amended and restated our existing senior credit facility in order to extend the maturities of our outstanding debt, obtain greater financial flexibility and take advantage of favorable debt capital markets to reduce our borrowing costs. The new senior credit facility allowed us to borrow an aggregate principal amount of $450.0 million, consisting of a $200.0 million revolving credit facility and a $250.0 million term loan facility. We used the proceeds of $250.0 million from the term loan facility and a $92.0 million borrowing under the revolving credit facility to repay amounts outstanding under the previously existing senior credit facility of $333.0 million, plus accrued interest and to pay related fees and expenses. Our credit facility is guaranteed by all our existing and future domestic wholly owned subsidiaries. Our credit facility also allows us to increase our revolving credit facility by up to $12 million and increase our term loan facility by up to $100 million, subject to certain limitations and satisfaction of certain conditions, including compliance with financial covenants. On August 1, 2006, we exercised this option and increased our revolving credit facility by $12 million and our existing term loan facility by $38 million in order to fund our stock repurchase plan and the repurchase of shares from Warburg Pincus. At December 31, 2006 our outstanding indebtedness was $350.3 million. Our credit facility includes a letter of credit subfacility of which $3.9 million of letters of credit was outstanding at December 31, 2006.

In addition to the above described credit facility, our foreign subsidiaries maintain local credit facilities to provide credit for overdraft, working capital and other purposes.

We are currently in compliance with all of the covenants and conditions under our credit facility. We believe that existing cash balances and internally generated cash flows, together with borrowings available under our revolving credit facility, will be sufficient to fund normal working capital needs, capital spending requirements, debt service requirements and dividend payments for at least the next twelve months. In addition, we believe that we will have adequate funds available to meet long-term cash requirements and that we will be able to comply with the covenants under the credit agreement. Future principal debt payments may be paid out of cash flows from operations, from future refinancing of our debt or from equity issuances. However, our ability to make scheduled payments of principal, to pay interest on or to refinance our indebtedness, to satisfy our other debt obligations and to pay dividends to stockholders will depend upon our future operating performance, which will be affected by general economic, financial, competitive, legislative, regulatory, business and other factors beyond our control.

Contractual Obligations

The following summarizes our fixed long-term contractual cash obligations as of December 31, 2006 (in thousands):

	Payments due by period				
	Less than 1 year	1 to 3 years	3 to 5 years	More than 5 years	Total
Long-term debt	$ 27,542	$ 54,550	$ 140,539	$ 253,077	$ 475,708
Operating leases	10,213	17,089	10,308	7,816	45,426
Purchase commitments	827				827
Pension plan contributions	5,813	2,251			8,064
Postretirement benefit plan obligations	1,684	3,463	4,119	11,376	20,642
Total	$ 46,079	$ 77,353	$ 154,966	$ 272,269	$ 550,667

Contractual obligations for long-term debt include principal and interest payments. Interest has been included at either the fixed rate or the variable rate in effect as of December 31, 2006, as applicable.

Environmental Matters

Our past and present business operations and the past and present ownership and operation of manufacturing plants on real property are subject to extensive and changing federal, state, local and foreign environmental laws and regulations, including those relating to discharges to air, water and land, the handling and disposal of solid and hazardous waste and the cleanup of properties affected by hazardous substances. As a result, we are involved from time to time in administrative and judicial proceedings and inquiries relating to environmental matters and could become subject to fines or penalties related thereto. We cannot predict what environmental legislation or regulations will be enacted in the future, how existing or future laws or regulations will be administered or interpreted or what environmental conditions may be found to exist. Compliance with more stringent laws or regulations, or stricter interpretation of existing laws, may require additional expenditures by us, some of which may be material. We have been identified as a potentially responsible party pursuant to the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) for remediation costs associated with waste disposal sites that we previously used. The remediation costs and our allocated share at some of these CERCLA sites are unknown. We may also be subject to claims for personal injury or contribution relating to CERCLA sites. We reserve amounts for such matters when expenditures are probable and reasonably estimable.

Off-Balance Sheet Arrangements

We do not currently have, nor have we ever had, any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. In addition, we do not engage in trading activities involving non-exchange traded contracts. As a result, we are not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in these relationships.

Section 404 of the Sarbanes-Oxley Act of 2002

Beginning in late 2004, we began a process to document and evaluate our internal controls over financial reporting in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 and the related regulations, which require annual management assessments of the effectiveness of our internal controls over financial reporting and a report by our independent auditors addressing these assessments. In this regard, management has dedicated internal resources, engaged outside consultants and adopted and implemented a detailed work plan to (i) assess and document the adequacy of internal controls over financial reporting, (ii) take steps to improve control processes, where appropriate, (iii) validate through testing that controls are functioning as documented and (iv) implement a continuous reporting and improvement process for internal control over financial reporting. Our efforts to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and the related regulations regarding our assessment of our internal controls over financial reporting have resulted, and are likely to continue to result, in increased expenses. We spent approximately $3 million in 2005 on Section 404 compliance related expenses. Section 404 compliance related expenses in 2006 were approximately $0.9 million.

Management and our audit committee have given our compliance with Section 404 the highest priority. We cannot be certain that these measures will ensure that we implement and maintain adequate controls over our financial processes and reporting in the future. Any failure to implement required new or improved controls, or difficulties encountered in their implementation, could harm our operating results or cause us to fail to meet our reporting obligations. If we fail to correct any issues in the design or operating effectiveness of internal controls over financial reporting or fail to prevent fraud, current and potential stockholders could lose confidence in our financial reporting, which could harm our business and the trading price of our common stock.

Forward-looking Statements

This annual report on Form 10-K contains forward-looking statements, principally in the sections entitled Quantitative and Qualitative Disclosures About Market Risk, Management s Discussion and Analysis of Financial Condition and Results of Operations , Risk Factors and Business. Statements and financial discussion and analysis contained in this annual report on Form 10-K that are not historical facts are forward-looking statements. These statements discuss goals, intentions and expectations as to future trends, plans, events, results of operations or financial condition, or state other information relating to us, based on our current beliefs as well as assumptions made by us and information currently available to us. Forward-looking statements generally will be accompanied by words such as anticipate , believe , could , estimate , expect , forecast , intend , may , possible , potential , predict , project , or other similar words, phrases or expressions. Although we belie forward-looking statements are reasonable, they are based upon a number of assumptions concerning future conditions, any or all of which may ultimately prove to be inaccurate. Important factors that could cause actual results to differ materially from the forward-looking statements include, without limitation: the risks described under Item 1A and in Item 7A of this annual report on Form 10-K; changes in the financial stability of our clients resulting in decreased corporate spending and service sector employment; changes in relationships with clients; the mix of products sold and of clients purchasing our products; the success of new technology initiatives; changes in business strategies and decisions; competition from our competitors; our ability to recruit and retain an experienced management team; changes in raw material prices and availability; restrictions on government spending resulting in fewer sales to one of our largest customers; our debt restrictions on spending; our ability to protect our patents, copyrights and trademarks; our reliance on furniture dealers to produce sales; lawsuits arising from patents, copyrights and trademark infringements; violations of environment laws and regulations; potential labor disruptions; adequacy of our insurance policies; the availability of future capital; and currency rate fluctuations. The factors identified above are believed to be important factors (but not necessarily all of the important factors) that could cause actual

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results to differ materially from those expressed in any forward-looking statement. Unpredictable or unknown factors could also have material adverse effects on us. All forward-looking statements included in this annual report on Form 10-K are expressly qualified in their entirety by the foregoing cautionary statements. Except as required under the Federal securities laws and the rules and regulations of the SEC, we undertake no obligation to update, amend, or clarify forward-looking statements, whether as a result of new information, future events, or otherwise.

Recent Accounting Pronouncements

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48), which is an interpretation of SFAS No. 109.

FIN 48 creates a single model to address uncertainty in tax positions, and clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS 109 by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in an enterprise s financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition.

FIN 48 is effective for fiscal years beginning after December 15, 2006. The cumulative effect of adopting FIN 48 will be recorded in retained earnings and other accounts, as applicable. We are currently evaluating the impact of FIN 48, which must be implemented effective January 1, 2007.

In September 2006, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB No. 87, 88, 106, and 132(R) (SFAS 158). Statement 158 requires plan sponsors of defined benefit pension and other postretirement benefit plans (collectively, postretirement benefit plans) to recognize the funded status of their postretirement benefit plans in the statement of financial position, measure the fair value of plan assets and benefit obligations as of the date of the fiscal year-end statement of financial position, and provide additional disclosures. On December 31, 2006, we adopted the recognition and disclosure provision of Statement 158. The effect of adopting Statement 158 on our financial condition at December 31, 2006 has been included in the accompanying consolidated financial statements. The requirement to measure plan assets and benefit obligations as of the date of the employers fiscal year-end statements of financial position is effective for us for the fiscal year ended December 31, 2008. See Note 14 to our consolidated financial statements for further discussion of the effect of adopting Statement 158 on our consolidated financial statements.

Item 7A. ***Quantitative And Qualitative Disclosures About Market Risk***

During the normal course of business, we are routinely subjected to market risk associated with interest rate movements and foreign currency exchange rate movements. Interest rate risk arises from our debt obligations and related interest rate hedge agreements. Foreign currency exchange rate risk arises from our non-U.S. operations and purchases of inventory from foreign suppliers.

We also have risk in our exposure to certain material and transportation costs. Our largest raw material costs are for steel and plastics. Steel is the primary raw material used in the manufacture of our products. The prices of plastic, another significant raw material used in the manufacture of our products, are sensitive to the cost of oil, which has increased significantly in recent history. For the year ended December 31, 2006 material inflation was approximately $12.8 million and transportation inflation was approximately $1.9 million. During 2005, our materials inflation increased by approximately $14.6 million and transportation costs increased approximately $6.6 million. Our material inflation increase was $8.9 million in 2004. We continue working to attempt to offset these price changes in raw materials and transportation through our global sourcing initiatives, cost improvements and price increases to our products.

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Interest Rate Risk

We have both fixed and variable rate debt obligations that are denominated in U.S. dollars. Changes in interest rates have different impacts on the fixed and variable-rate portions of the debt. A change in interest rates impacts the interest incurred and cash paid on the variable-rate debt but does not impact the interest incurred or cash paid on the fixed rate debt. The weighted average rate for 2006 was 7.2%. The weighted average rate for the same period of 2005 was 6.4%.

We use interest rate hedge agreements for other than trading purposes in order to manage our exposure to fluctuations in interest rates on our variable-rate debt. Such agreements effectively convert $200.0 million of our variable-rate debt to a fixed-rate basis, utilizing the three-month London Interbank Offered Rate, or LIBOR, as a floating rate reference. Fluctuations in LIBOR affect both our net financial instrument position and the amount of cash to be paid or received by us, if any, under these agreements.

The following table summarizes our market risks associated with our debt obligations and interest rate hedge agreements as of December 31, 2006. For debt obligations, the table presents principal cash flows and related weighted average interest rates by year of maturity. Variable interest rates presented for variable-rate debt represent the weighted average interest rates on our credit facility borrowings as of December 31, 2006. For interest rate caps, the table presents the notional amounts and related weighted average interest rates by year of maturity.

	2007	2008	2009	2010	2011	Thereafter	Total	Fair Value
				(dollars in thousands)				
Rate Sensitive Liabilities								
Long-term Debt:								
Fixed Rate	$ 116	$ 121	$ 125	$ 130	$ 139	$	$ 631	$ 631
Average Interest Rate	4.11%	4.11%	4.11%	4.11%	4.11%			
Variable Rate	$ 2,880	$ 2,880	$ 2,880	$ 97,880	$ 2,880	$ 240,285	$ 349,685	$ 349,685
Average Interest Rate	7.04%	7.04%	7.04%	7.04%	7.04%	7.04%		
Rate Sensitive Derivative Financial Instruments								
Interest Rate Caps:								
Notional Amount		$ 200,000					$ 200,000	$ 71
Strike Rate		6.00%						

An increase in interest rates of 1% would increase annual interest expense by approximately $3.5 million. We will continue to review its exposure to interest rate fluctuations and evaluate whether it should manage such exposure through derivative transactions.

Foreign Currency Exchange Rate Risk

We manufacture our products in the United States, Canada and Italy, and sell our products primarily in those markets as well as in other European countries. Our foreign sales and certain expenses are transacted in foreign currencies. Our production costs, profit margins and competitive position are affected by the strength of the currencies in countries where we manufacture or purchase goods relative to the strength of the currencies in countries where our products are sold. Additionally, as we report currency in the U.S. dollar, our financial position is affected by the strength of the currencies in countries where we have operations relative to the strength of the U.S. dollar. The principal foreign currencies in which we conduct business are the Canadian dollar and the Euro. Approximately 11.3% and 11.5% of our revenues in 2006 and 2005, respectively, and 36.7% and 36.1% of our cost of goods sold in 2006 and 2005, respectively, were denominated in currencies other than the U.S. dollar. Foreign currency exchange rate fluctuations resulted in a $0.6 million gain in 2006 and a $2.3 million loss in 2005.

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From time to time, we enter into foreign currency forward exchange contracts and foreign currency option contracts for other than trading purposes in order to manage our exposure to foreign exchange rates associated with short-term operating receivables of a Canadian subsidiary that are payable by our U.S. operations. The terms of these contracts are generally less than a year. Changes in the fair value of such contracts are reported in earnings in the period the value of the contract changes. The net gain or loss upon settlement and the remaining change in fair value is recorded as a component of other income (expense). The fair market value of the foreign currency option contract outstanding at December 31, 2006 was $92 thousand and is included in other current liabilities in our consolidated balance as of December 31, 2006. During 2006, we recognized a net gain of $744 thousand related to various foreign currency option contracts initiated and settled during 2006. As of December 31, 2005, we had no outstanding foreign currency contracts, however, we recorded during the year an $87 thousand unrecognized loss related to the termination of a foreign currency contract outstanding at December 31, 2004. The fair market value of the contract outstanding at December 31, 2004 was included in prepaid and other current assets in our consolidated balance sheet.

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Item 8. ***Financial Statements and Supplementary Data***

KNOLL, INC.

CONSOLIDATED BALANCE SHEET

DECEMBER 31, 2006 AND 2005

(dollars in thousands, except share and per share data)

	2006	2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 16,038	$ 10,695
Customer receivables, net	132,970	113,531
Inventories	75,930	56,500
Deferred income taxes	13,416	9,156
Prepaid and other current assets	10,030	7,867
Total current assets	248,384	197,749
Property, plant, and equipment, net	137,729	142,166
Goodwill, net	44,637	45,333
Intangible assets, net	193,654	191,066
Other non-trade receivables	3,835	4,827
Other noncurrent assets	3,898	1,405
Total Assets	$ 632,137	$ 582,546
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Current maturities of long-term debt	$ 2,996	$ 2,599
Accounts payable	72,567	56,559
Income taxes payable	16,317	10,253
Other current liabilities	79,334	64,345
Total current liabilities	171,214	133,756
Long-term debt	347,320	313,439
Deferred income taxes	41,665	44,082
Postretirement benefits other than pensions	26,636	23,864
Pension liability	27,633	16,908
International retirement obligation	5,243	5,201
Other noncurrent liabilities	8,042	7,580
Total liabilities	627,753	544,830
Stockholders equity:		
Common stock, $0.01 par value; 200,000,000 shares authorized; 49,037,660 issued and outstanding (net of 6,348,764 treasury shares) in 2006 and 52,338,171 shares issued and outstanding (net of 300,008 treasury shares) in 2005	490	523
Additional paid-in-capital	4,409	82,072
Unearned stock grant compensation		(20,720)
Accumulated deficit	(2,726)	(32,914)
Accumulated other comprehensive income	2,211	8,755

Total stockholders equity	4,384	37,716
Total Liabilities and Stockholders Equity	$ 632,137	$ 582,546

See accompanying notes to the consolidated financial statements

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KNOLL, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 2006, 2005, AND 2004

(dollars in thousands, except share and per share data)

	2006	2005	2004
Sales	$ 982,152	$ 807,960	$ 706,390
Cost of sales	663,115	535,904	465,379
Gross profit	319,037	272,056	241,011
Selling, general, and administrative expenses	202,097	179,217	169,706
Operating Income	116,940	92,839	71,305
Interest expense	23,717	23,684	19,452
Other income (expense), net	741	(5,355)	(5,316)
Income before income tax expense	93,964	63,800	46,537
Income tax expense	35,331	27,891	19,793
Net Income	$ 58,633	$ 35,909	$ 26,744
Net earnings per share			
Basic	$ 1.18	$ 0.70	$ 0.58
Diluted	$ 1.14	$ 0.68	$ 0.55
Weighted-average shares outstanding:			
Basic	49,606,677	51,219,123	46,353,253
Diluted	51,238,088	52,919,388	48,319,483

See accompanying notes to the consolidated financial statements

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KNOLL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

YEARS ENDED DECEMBER 31, 2006, 2005, AND 2004

(dollars in thousands, except share and per share data)

	Common Stock	Additional Paid-In Capital	Unearned Stock Grant Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholder s Equity (Deficit)
Balance at January 1, 2004	$ 463	$ 1,937	$	$ (12,068)	$ 1,549	$ (8,119)
Net income				26,744		26,744
Foreign currency translation adjustment					8,501	8,501
Unrealized gain on derivative (net of income tax effect of $101)					150	150
Minimum pension liability (net of income tax effect of $1,629)					2,443	2,443
Total comprehensive income						37,838
Shares for consideration:						
Exercise of stock options, including tax benefit of $5,501 (1,581,706 shares)	16	19,574				19,590
Shares issued under stock incentive plan (1,600,000 shares)	16	23,984	(24,000)			
Earned stock grant compensation			167			167
Cash Dividend ($1.525 per share)				(70,601)		(70,601)
Purchase of common stock (13,200 shares)		(220)				(220)
Balance at December 31, 2004	$ 495	$ 45,275	$ (23,833)	$ (55,925)	$ 12,643	$ (21,345)
Net income				35,909		35,909
Foreign currency translation adjustment					272	272
Unrealized gain on derivative (net of income tax effect of $151)					232	232
Minimum pension liability (net of income tax effect of $2,862)					(4,392)	(4,392)
Total comprehensive income						32,021
Shares issued for consideration:						
Exercise of stock options, including tax benefit of $8,347 (2,990,262 shares)	29	38,850				38,879
Shares issued under stock incentive plan (50,000 shares)	1	938	(939)			
Shares issued under employee stock purchase plan (3,953 shares)		65				65
Earned stock grant compensation			4,052			4,052
Cash dividend ($.25 per share)				(12,898)		(12,898)
Purchase of common stock (181,408 shares)	(2)	(3,056)				(3,058)
Balance at December 31, 2005	$ 523	$ 82,072	$ (20,720)	$ (32,914)	$ 8,755	$ 37,716
Net income				58,633		58,633
Foreign currency translation adjustment					1,714	1,714
Unrealized loss on derivative (net of income tax effect of $250)					(382)	(382)

Minimum pension liability (net of income tax effect of $1,856)					2,849	2,849
Total comprehensive income						62,814
Shares issued for consideration:						
Exercise of stock options, including tax benefit of $10,158 (2,808,812 shares)	28	38,608				38,636
Shares issued under employee stock purchase plan (3,433 shares)		66				66
Stock-based compensation, net of forfeitures (64,000 shares)	(1)	4,505				4,504
Cash dividend ($.41 per share)				(20,830)		(20,830)
Purchase of common stock (6,048,756 shares)	(60)	(100,122)		(7,615)		(107,797)
Reclassification of unearned compensation due to the adoption of FASB 123R		(20,720)	20,720			
Adjustment to initially apply FASB Statement No. 158 (net of tax of $6,987)					(10,725)	(10,725)
Balance at December 31, 2006	$ 490	$ 4,409	$	$ (2,726)	$ 2,211	$ 4,384

See accompanying notes to the consolidated financial statements

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KNOLL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2006, 2005, AND 2004

(in thousands)

	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$ 58,633	$ 35,909	$ 26,744
Adustments to reconcile net income to cash provided by operating activities:			
Depreciation	19,194	18,721	20,080
Amortization of intangible assets	663	626	1,692
Write-off of deferred financing fees		3,562	2,518
Unrealized foreign currency loss	157	2,045	2,944
Premium paid for interest rate cap agreement	(204)		(425)
Tax benefit from exercise of stock options		8,347	5,501
Stock based compensation	4,504	4,052	167
Other non-cash items	1,230	(5)	(65)
Changes in assets and liabilities:			
Customer receivables	(17,268)	(16,559)	299
Inventories	(18,866)	(7,304)	(9,932)
Accounts payable	14,176	11,318	(9,847)
Current and deferred income taxes	(668)	9,360	8,125
Other current assets	(2,053)	(1,560)	2,503
Other current liabilities	13,882	3,068	7,883
Other noncurrent assets and liabilities	4,148	5,861	2,116
Cash provided by operating activities	77,528	77,441	60,303
CASH FLOWS FOR INVESTING ACTIVITIES			
Capital expenditures	(13,362)	(10,744)	(13,131)
Purchase of a trademark and other intangible asset	(3,250)		
Proceeds from the sale of assets	34	101	
Cash used in investing activities	(16,578)	(10,643)	(13,131)
CASH FLOWS FOR FINANCING ACTIVITIES			
Proceeds from the issuance of long-term debt	38,000	250,000	425,000
Proceeds (repayment) from revolving credit facilities, net	29,000	66,000	(223,750)
Repayment of long-term debt	(32,827)	(392,723)	(189,354)
Deferred financing fees		(3,280)	(5,819)
Payment of dividends	(20,195)	(12,490)	(70,601)
Proceeds from the issuance of common stock	27,249	31,390	13,216
Purchase of common stock for treasury	(107,799)	(3,056)	(220)
Tax benefit from the exercise of stock options	10,158		
Cash used in financing activities	(56,414)	(64,159)	(51,528)
Effect of exchange rate changes on cash and cash equivalents	807	(996)	1,891
Increase (decrease) in cash and cash equivalents	5,343	1,643	(2,465)

Cash and cash equivalents at beginning of period	10,695	9,052	11,517
Cash and cash equivalents at end of period	$ 16,038	$ 10,695	$ 9,052

See accompanying notes to the consolidated financial statements

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KNOLL, INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2006

1. NATURE OF OPERATIONS

Knoll, Inc. and its subsidiaries (the Company or Knoll) are engaged in the design, manufacture and sale of office furniture products and accessories, focusing on the middle to high-end segments of the contract furniture market. The Company has operations in the United States (U.S.), Canada and Europe and sells its products primarily through its direct sales representatives and independent dealers.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements of the Company include the accounts of Knoll, Inc. and its wholly owned subsidiaries. Intercompany transactions and balances have been eliminated in consolidation.

The results of the European subsidiaries are reported and included in the consolidated financial statements on a one-month lag to allow for the timely preparation of consolidated information. The effect of this presentation is not material to the financial statements.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and highly liquid investments with maturities of three months or less at the date of purchase.

Revenue Recognition and Accounts Receivable

Revenue from the sale of products is recognized upon transfer of title to the client, which occurs at the time of shipment.

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its clients and dealers to make required payments. The allowance is determined through an analysis of the aging of accounts receivable and assessments of risk that are based on historical trends and an evaluation of the impact of current and projected economic conditions. The Company evaluates the past-due status of its trade receivables based on the contractual terms of sale. If the financial condition of the Company s clients and dealers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. Accounts receivable are charged off against the allowance for doubtful accounts when the Company determines that recovery is unlikely. Losses have been consistent with the Company s expectations.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out method.

Property, Plant, Equipment and Depreciation

Property, plant, and equipment are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. The useful lives are as follows: 45 years for buildings and 3 to 12 years for machinery and equipment.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Intangible Assets

Intangible assets consist of goodwill, trademarks and deferred financing fees. Goodwill is recorded at the amount by which cost exceeds the net assets of acquired businesses, and all other intangible assets are recorded at cost.

Goodwill and other intangible assets are tested for impairment at least annually rather than being amortized. The Company determined that no impairment existed based on the impairment tests for each year through 2006.

On December 19, 2006, the Company purchased certain intangible assets as an investment in its seating line. A definite useful life was assigned to these intangibles and as such amortization will be recorded over the economic life of the intangibles in accordance with Statement of Financial Accounting Standards 142 Goodwill and Other Intangible Assets .

Deferred financing costs that are incurred by the Company in connection with the issuance of debt are deferred and amortized to interest expense over the life of the underlying indebtedness.

Shipping and Handling

Amounts billed to clients for shipping and handling of products are classified as sales in the consolidated statements of operations. Costs incurred by the Company for shipping and handling are classified as cost of sales.

Research and Development Costs

Research and development expenses, which are expensed as incurred, were $12.7 million for 2006, $10.8 million for 2005, and $12.8 million for 2004.

Income Taxes

Deferred tax assets and liabilities are recognized for the future income tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and are measured using enacted tax rates expected to apply to taxable income in the years in which the temporary differences are expected to reverse.

Fair Value of Financial Instruments

The fair values of cash and cash equivalents, accounts receivable, and accounts payable, approximate their carrying amounts due to their immediate or short-term periods to maturity. The stated interest rates on the Company s long-term debt approximate market rates for debt instruments with similar terms and maturities, and accordingly, the fair value of the Company s long-term debt, described in Note 8, approximates its carrying amount. The derivative instruments described in Note 10, are recorded at fair value as estimated by the dealer.

Derivative Financial Instruments

The Company uses derivative financial instruments to reduce its exposure to adverse fluctuations in foreign currency exchange and interest rates. In accordance with Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities , on the date a derivative instrument is entered into, the Company designates the derivative as (i) a fair value hedge, (ii) a cash flow hedge, (iii) a hedge of a net investment in a foreign operation, or (iv) a risk management instrument. The Company recognizes all derivatives

KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

on the consolidated balance sheet at fair value. On September 30, 2006, the Company entered into two new interest rate cap agreements. These agreements were classified as risk management instruments and management elected to not apply hedge accounting. As such, the change in fair value of the contracts is reported in earnings in the period the value of the contract changes as a component of other income (expense). The interest rate swap agreement entered into in October 2004 (see further discussion in Note 10) was classified as a cash flow hedge and as such the effective portion of the change in the value of the contracts is recorded in other comprehensive income, net of tax, and reclassified into earnings in the period or periods during which the hedged transactions affect earnings. Any ineffective portion of the change in the value of the October 2004 contract was immediately recognized in earnings. The Company also entered into an interest rate cap agreement in October 2004. The Company also classified this agreement as a risk management instrument and elected to not apply hedge accounting.

Foreign Currency Translation

Results of foreign operations are translated into U.S. dollars using average exchange rates during the period, while assets and liabilities are translated into U.S. dollars using exchange rates in effect at the balance sheet date. The resulting translation adjustments are recorded in accumulated other comprehensive income. As of December 31, 2006 and 2005, the accumulated foreign currency translation adjustments included in other comprehensive income amounted to $14.5 million and $12.8 million, respectively. Transaction gains and losses resulting from exchange rate changes on transactions denominated in currencies other than the functional currency are included in income in the period in which the change occurs.

Stock-Based Compensation

At December 31, 2006, the Company has two stock incentive plans, which are described more fully in Note 15. The Company adopted the revision of Statement of Financial Accounting Standards (SFAS) No. 123, *Share-Based Payment* (SFAS 123(R)) on January 1, 2006. SFAS 123R supersedes SFAS No. 123 and Accounting Principles Board Opinion No. 25 (APB 25). Under SFAS 123(R) the Company measures the cost of employees services received in exchange for stock options based on the grant-date fair value of the award, with such costs recognized over the applicable vesting period. The Company applied SFAS 123(R) using the modified prospective method which applies to all stock options granted after the Company s initial public offering in December 2004. For all options issued prior to the Company s initial public offering and which were historically accounted for under the minimum value method, the prospective method was applied and such options continue to be accounted for under the provisions of APB 25. Under APB 25, no stock-based employee compensation costs is reflected in net income, as all options granted during that time period have an exercise price equal to the fair value of the underlying common stock on the date of grant. Under the modified prospective method, the results of operations of prior periods have not been restated. Accordingly, the Company will continue to provide pro forma financial information for prior periods to illustrate the effect on net income and earnings per share of applying the fair value recognition provisions of SFAS No. 123.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table illustrates the effect on net income if the Company had applied the fair value recognition provisions of SFAS 123 to all of its stock-based employee compensation.

	Twelve Months Ended December 31,		
	2006	2005	2004
	(in thousands except per share data)		
Net income, as reported	$ 58,633	$ 35,909	$ 26,744
Add:			
Stock-based employee compensation expense included in reported net income	6,476	4,664	914
Deduct:			
Total stock-based employee compensation expense determined under fair-value-based method, net of related tax effects	(7,173)	(6,753)	(2,884)
As adjusted net income	$ 57,936	$ 33,820	$ 24,774
Earnings per share:			
Basic as reported	$ 1.18	$ .70	$ .58
Diluted as reported	$ 1.14	$ .68	$ .55
Basic as adjusted	$ 1.17	$ .66	$ .53
Diluted as adjusted	$ 1.13	$ .64	$ .51

For the year ended December 31, 2006, the Company recognized $6.5 million of compensation expense which includes an additional $697 thousand of stock option expense as a result of adopting Statement 123(R). Prior to the adoption of SFAS 123(R), the Company included all tax benefits associated with stock-based compensation as operating cash flows in the consolidated statement of cash flows. SFAS 123(R) requires any reduction in taxes payable resulting from tax deductions that exceed the recognized compensation expense (excess tax benefit) to be classified as financing cash flows. The Company included $10.2 million of excess tax benefits in the Company s cash flows from financing activities for the twelve months ended December 31, 2006 that would have been classified as operating cash flows had the Company not adopted SFAS 123(R). Lastly, upon adoption of SFAS 123(R), the Company reduced unearned stock compensation and paid-in capital by $20.7 million on the consolidated balance sheet.

Prior to 2005, the fair value of the options was estimated using a minimum value method for grants made on or subsequent to March 24, 1999 and through December 14, 2004. The Company went public on December 14, 2004 and used the Black-Scholes option pricing model to value options granted after that date. During 2005, the Company replaced the Black-Scholes option pricing model with a lattice model in preparation for the implementation of FAS 123(R) effective January 1, 2006. For stock options granted after December 14, 2004 and during 2005 and 2006 the following assumptions shown in the table below were used in the lattice model.

Because lattice based option valuation models incorporate ranges of assumptions for inputs, those ranges are disclosed. Expected volatilities are based on implied volatilities from traded options on the Company s stock, historical volatilities of the Company s and competitors stocks, and other factors. The Company uses historical data to estimate option exercise and employee termination within the valuation model. The expected term of options granted is derived based on the mid-point between the vesting date and the end of the contractual term. The risk-free rate for periods within the contractual life of the option is based on the 10-year U.S. Treasury yield curve in effect at the time of grant.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	2006	2005	2004
Expected volatility	29%	22%	22%
Expected dividend yield	2.00%	2.30%	2.30%
Expected Term (in years)	7	7	7
Risk-free rate	4.59%	4.09-4.49%	4.21%

Accumulated Other Comprehensive Income (Loss)

The components of accumulated other comprehensive income (loss), net of tax, if applicable, are as follows (in thousands):

	Beginning Balance	Before-Tax Amount	Tax Benefit (Expense)	Net-of-Tax Amount	Ending Balance
December 31, 2004					
Minimum pension liability	$ (2,450)	$ 4,072	$ (1,629)	$ 2,443	$ (7)
Foreign currency translation adjustment	3,999	8,501		8,501	12,500
Unrealized gain on derivative		251	(101)	150	150
Accumulated other comprehensive income (loss), net of tax	$ 1,549	$ 12,824	$ (1,730)	$ 11,094	$ 12,643
December 31, 2005					
Minimum pension liability	$ (7)	$ (7,254)	$ 2,862	$ (4,392)	$ (4,399)
Foreign currency translation adjustment	12,500	272		272	12,772
Unrealized gain on derivative	150	383	(151)	232	382
Accumulated other comprehensive income (loss), net of tax	$ 12,643	$ (6,599)	$ 2,711	$ (3,888)	$ 8,755
December 31, 2006					
Pension funded status adjustment	$ (4,399)	$ (13,007)	$ 5,131	$ (7,876)	$ (12,275)
Foreign currency translation adjustment	12,772	1,714		1,714	14,486
Unrealized gain on derivative	382	(632)	250	(382)	
Accumulated other comprehensive income (loss), net of tax	$ 8,755	$ (11,925)	$ 5,381	$ (6,544)	$ 2,211

Earnings per Share

Basic earnings per share excludes the dilutive effect of common shares that could potentially be issued, due to the exercise of stock options, and is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted earnings per share includes the effect of shares and potential shares issued under the stock incentive plans.

	Twelve Months Ended December 31,		
	2006	2005	2004

	(in thousands)		
Weighted average shares of common stock outstanding basic	49,607	51,219	46,353
Potentially dilutive shares resulting from stock plans	1,631	1,700	1,966
Weighted average common shares diluted	51,238	52,919	48,319
Antidilutive options not included in the weighted average common shares-diluted calculation	25	295	1,590

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of certain assets, liabilities, revenues and expenses and the disclosure of certain contingent assets and liabilities. Actual results may differ from such estimates.

New Accounting Pronouncements

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), which is an interpretation of SFAS No. 109.

FIN 48 creates a single model to address uncertainty in tax positions, and clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS 109 by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in an enterprise s financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition.

FIN 48 is effective for fiscal years beginning after December 15, 2006. The cumulative effect of adopting FIN 48 will be recorded in retained earnings and other accounts, as applicable. The Company is currently evaluating the impact of FIN 48, which must be implemented effective January 1, 2007.

In September 2006, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB No. 87, 88, 106, and 132(R)* (SFAS 158). Statement 158 requires plan sponsors of defined benefit pension and other postretirement benefit plans (collectively, postretirement benefit plans) to recognize the funded status of their postretirement benefit plans in the statement of financial position, measure the fair value of plan assets and benefit obligations as of the date of the fiscal year-end statement of financial position, and provide additional disclosures. On December 31, 2006, the Company adopted the recognition and disclosure provision of Statement 158. The effect of adopting Statement 158 on the Company s financial condition at December 31, 2006 has been included in the accompanying consolidated financial statements. The requirement to measure plan assets and benefit obligations as of the date of the employer s fiscal year-end statements of financial position is effective for the Company for the fiscal year ended December 31, 2008. See Note 14 for further discussion of the effect of adopting Statement 158 on the Company s consolidated financial statements.

3. CUSTOMER RECEIVABLES

Customer receivables are presented net of an allowance for doubtful accounts of $3,337,000 and $3,826,000 at December 31, 2006 and 2005, respectively. Management performs ongoing credit evaluations of its clients and generally does not require collateral. As of December 31, 2006 and 2005, the U.S. government and agencies thereof, represented approximately 18.4% and 15.4%, respectively, of gross customer receivables.

4. INVENTORIES

	2006	**2005**
	(in thousands)	
Raw materials	$ 44,114	$ 32,769
Work in process	7,952	6,080
Finished goods	23,864	17,651
Inventories	$ 75,930	$ 56,500

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Inventory reserves for obsolescence and other estimated losses were $6,462 and $5,031 at December 31, 2006 and 2005, respectively.

5. PROPERTY, PLANT, AND EQUIPMENT

	2006	2005
	(in thousands)	
Land and buildings	$ 88,269	$ 86,177
Machinery and equipment	290,107	281,177
Construction in progress	5,886	3,189
Property, plant and equipment	384,262	370,543
Accumulated depreciation	(246,533)	(228,377)
Property, plant and equipment, net	$ 137,729	$ 142,166

6. INTANGIBLE ASSETS

Information regarding the Company s goodwill and other intangible assets follows (in thousands):

	2006			2005		
	Gross Amount	Accumulated Amortization	Net Amount	Gross Amount	Accumulated Amortization	Net Amount
Unamortizable intangible assets:						
Goodwill	$ 53,049	$ (8,412)	$ 44,637	$ 53,745	$ (8,412)	$ 45,333
Trademarks	219,900	(32,069)	187,831	219,900	(32,069)	187,831
Amortizable intangible assets:						
Deferred financing fees	3,401	(828)	2,573	3,401	(166)	3,235
Trademarks	3,000		3,000			
Other	250		250			
Total	$ 279,600	$ (41,309)	$ 238,291	$ 277,046	$ (40,647)	$ 236,399

On December 19, 2006, the Company entered an agreement to purchase the rights to the LIFE trademark associated with its LIFE chair for $3,000,000. The Company assigned an 11 year useful life to the trademark and will amortize it based on a percentage of LIFE chair sales through 2017.

The Company will evaluate annually whether the estimated useful life of the trademark warrants revisions and any such changes will be applied prospectively.

On October 3, 2005, the Company amended and restated its existing senior credit facility. As a result of this transaction, approximately $3,562,000 of deferred financing fees, net of accumulated amortization, were written off and approximately $3,280,000 of new deferred financing fees were recorded.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company recorded amortization of deferred financing fees of approximately $663,000, $626,000, and $1,692,000 for the years ended December 31, 2006, 2005 and 2004, respectively. This amortization was recorded as a component of interest expense. Estimated amortization expense for each of the five succeeding years is as follows:

2007	$ 1,263
2008	1,273
2009	1,238
2010	968
2011	403

7. OTHER CURRENT LIABILITIES

	2006	2005
	(in thousands)	
Accrued employee compensation	$ 41,348	$ 33,619
Accrued pension costs	5,813	3,039
Customer deposits	6,786	6,950
Accrued warranty	7,436	5,521
Other	17,951	15,216
Other current liabilities	$ 79,334	$ 64,345

8. INDEBTEDNESS

The Company s long-term debt is summarized as follows:

	2006	2005
	(in thousands)	
Term loans, variable rate (7.11% at December 31, 2006 and 6.53% at December 31, 2005)	$ 254,685	$ 249,375
Revolving loans, variable rate (6.85% at December 31, 2006 and 6.331%-8.250% at December 31, 2005)	95,000	66,000
Other	631	663
Total	350,316	316,038
Less current maturities	(2,996)	(2,599)
Long-term debt	$ 347,320	$ 313,439

Term and Revolving Loans

On October 3, 2005, the Company amended and restated its existing senior credit facility. The new senior secured facility permits the Company to borrow an aggregate principal amount of up to $450 million, consisting of a $200 million revolving credit facility and a $250 million term loan facility. The Company used the proceeds of the term loan facility and a $92 million borrowing under the revolving credit facility to repay amounts outstanding under the previously existing senior credit facility of $333 million, plus accrued interest and to pay related fees and expenses.

Under the Company s credit agreement, the Company could increase its revolving credit facility by up to $12 million and increase its term loan facility by up to $100 million, subject to certain limitations and satisfaction

KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

of certain conditions, including compliance with certain financial covenants. On August 1, 2006, the Company exercised this option and increased its revolving credit facility by $12 million and its existing term loan facility by $38 million.

The term loan is subject to a 0.25% quarterly principal amortization equal to $720 thousand per quarter with the remaining principal due in October 2012. Loans made pursuant to the revolving credit facility may be borrowed, repaid and reborrowed from time to time until October 2010, subject to satisfaction of certain conditions on the date of any such borrowing. Obligations under the credit facility are currently secured by a first security interest in substantially all of the Company s assets and properties, as well as those of the Company s domestic subsidiaries. Following an improvement of the Company s debt ratings to specified levels, the indebtedness will be secured only by a pledge of the capital stock of each of the Company s wholly owned domestic subsidiaries and 65% of the capital stock of each of the Company s, and the wholly owned domestic subsidiaries , first tier international subsidiaries. Borrowings under the credit agreement bear interest at a floating rate based, at the Company s option, upon (i) a LIBOR rate plus an applicable percentage or (ii) the greater of the federal funds rate plus 0.5% or the prime rate, plus an applicable percentage.

The senior credit agreement contains a letter of credit subfacility that allows for the issuance of up to $15.0 million in letters of credit and a swing-line loan subfacility that allows for issuance of up to $10.0 million in swing-line loans. The amount available for borrowing under the revolving credit facility is reduced by the total outstanding letters of credit and swing-line loans. At December 31, 2006, the Company had approximately $3.9 million of letters of credit outstanding, $95.0 million outstanding under the revolving credit facility and approximately $113.1 million, available for borrowing under the revolving credit facility. The letters of credit have expiration dates of April 1, 2007 and August 31, 2007.

The Company is required to pay a commitment fee equal to 0.5% per annum on the unused portion of the revolving credit facility, subject to adjustment based upon the Company s leverage ratio. In addition, the Company is required to pay a letter of credit fee equal to the applicable margin payable on revolving credit facility loans maintained as LIBOR loans, subject to adjustment under similar circumstances.

In addition, the credit agreement also contains various affirmative and negative covenants that among other things, limit, subject to certain exceptions, the incurrence of additional indebtedness, capital expenditures in excess of a specified amount in any fiscal year (with a two-year carry-over), and declaration or payment of dividends and stock repurchases. The Company was in compliance with the credit agreement covenants at December 31, 2006.

The Company also has several revolving credit agreements with various European financial institutions. These credit agreements provide credit primarily for overdraft and working capital purposes. As of December 31, 2006, total credit available under such agreements was approximately $8,659,000. There is currently no expiration date on these agreements. The interest rates on borrowings are variable and are based on the monetary market rate that is linked to each country s prime rate. As of December 31, 2006, the Company had no outstanding borrowings under the European credit facilities.

Interest Paid

During 2006, 2005 and 2004, the Company made interest payments including amounts related to the Company s interest rate collar swap and cap agreements totaling $22,844,000, $24,670,000 and $17,081,000 respectively.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Maturities

Aggregate maturities of the Company s indebtedness as of December 31, 2006 are as follows (in thousands):

2007	$ 2,996
2008	3,001
2009	3,005
2010	98,010
2011	3,019
Subsequent years	240,285
	$ 350,316

9. PREFERRED STOCK

The Company s Certificate of Incorporation authorizes the issuance of 10,000,000 shares of preferred stock with a par value of $1.00 per share. Subject to applicable laws, the Board of Directors is authorized to provide for the issuance of preferred shares in one or more series, for such consideration and with designations, powers, preferences and relative, participating, optional or other special rights and the qualifications, limitations or restrictions thereof, as shall be determined by the Board of Directors. There is no Preferred Stock outstanding as of December 31, 2006 and 2005.

10. DERIVATIVE FINANCIAL INSTRUMENTS

The Company uses derivative financial instruments, to reduce its exposure to adverse fluctuations in foreign currency exchange and interest rates.

Interest Rate Swap and Cap Agreements

In October 2004, as required by the Company s credit facility, the Company entered into an interest rate swap agreement and an interest rate cap agreement for purposes of managing its risk in market interest rate fluctuations. These agreements hedge interest rate risk on a notional amount of approximately $212.5 million of the Company s borrowings under the credit facility. Under the interest rate swap agreement, the Company pays a fixed rate of interest of 3.010% and receives a variable rate of interest equal to three-month LIBOR, as determined on the last day of each quarterly settlement period on an aggregated notional principal amount of $50.0 million. Changes in the fair value of the interest rate swap agreement are recorded in the period the value of the contract changes. The net amount paid or received upon quarterly settlements is recorded as an adjustment to interest expense, while the change in fair value is recorded as a component of accumulated other comprehensive income in the equity section of the balance sheet. The interest rate cap agreement sets a maximum interest rate on a notional amount and utilizes LIBOR as a variable-rate reference. Under the cap agreement, the Company paid a premium of $425 thousand for a cap rate of 4.25% on $162.5 million of the Company s borrowing under the credit facility. The Company has elected not to apply hedge accounting under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities to the interest rate cap agreement. As such, the change in fair value of the contract is reported in earnings in the period the value of the contract changes as a component of other income (expense). Both the interest rate swap agreement and the interest rate cap agreement matured on September 29, 2006.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

On September 30, 2006, the Company entered into two new interest rate cap agreements. Under these agreements, the Company paid a total premium of approximately $204 thousand for a cap rate of 6.00% on $200 million of the Company s borrowings under the credit facility. The Company has elected not to apply hedge accounting under SFAS No. 133 to these agreements. As such, the change in fair value of the contracts is reported in earnings in the period the value of the contract changes as a component of other income (expense). The interest rate cap agreements mature on September 30, 2008.

The fair values of the Company s derivative instruments included in current assets are summarized as follows:

	2006	2005
	(in thousands)	
Interest rate swap	$	$ 634
Interest rate cap		570
	$	$ 1,204

The fair values of the Company s derivative instruments included in non-current assets are summarized as follows:

	2006	2005
	(in thousands)	
Interest rate cap agreements	$ 71	$
	$ 71	$

The change in the fair values of the Company s derivative instruments and the adjustment to interest expense are summarized as follows:

	2006	2005	2004
		(in thousands)	
Interest income (expense)	$ 1,674	$ 142	$ (966)
Other income (expense)	(703)	295	695
Pre-tax other comprehensive income (loss)	(632)	383	251
Aggregate net benefit (expense)	$ 339	$ 820	$ (20)

The Company will continue to review its exposure to interest rate fluctuations and evaluate whether it should manage such exposure through derivative transactions.

Foreign Currency Contracts

From time to time, the Company enters into foreign currency forward exchange contracts and foreign currency option contracts to manage its exposure to foreign exchange rates associated with short-term operating receivables of a Canadian subsidiary that are payable by the U.S. operations. The terms of these contracts are generally less than a year. Changes in the fair value of such contracts are reported in earnings in the period the value of the contract changes. The net gain or loss upon settlement and the remaining change in fair value is recorded as a component of other income (expense).

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The fair market value of the foreign of the foreign currency option contract outstanding at December 31, 2006 was $92 thousand and is included in other current liabilities in the Company s consolidated balance as of December 31, 2006. During 2006, the Company recognized a net gain of $744 thousand related to various foreign currency option contracts initiated and settled during 2006.

As of December 31, 2005, the Company had no outstanding foreign currency contracts, however, during the year the Company recorded an $87 thousand unrecognized loss related to the termination of a foreign currency contract outstanding at December 31, 2004. The fair market value of the outstanding contract on December 31, 2004 was included in prepaid and other current assets in the Company s consolidated balance sheet.

11. CONTINGENT LIABILITIES AND COMMITMENTS

The Company is currently involved in claims and matters of litigation, including environmental contingencies, arising in the ordinary course of business. The Company accrues for such matters when expenditures are probable and reasonably estimable. Management is of the opinion that such claims and litigation, based upon information presently known, either individually or in the aggregate, will not have a material adverse effect on the Company s consolidated financial position, results of operations or cash flows.

The Company offers a warranty for all of its products. The specific terms and conditions of those warranties vary depending upon the product sold. The Company estimates the costs that may be incurred under its warranties and records a liability in the amount of such costs at the time product revenue is recognized. Factors that affect the Company s liability include historical product-failure experience and estimated repair costs for identified matters for each specific product category. The Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary. Adjustments to recorded reserves for pre-existing warranties are not material for each period presented.

Changes in the Company s warranty reserve during the years ended December 31, 2006, 2005, and 2004 are as follows:

	2006	2005	2004
		(in thousands)	
Balance, beginning of the year	$ 5,521	$ 5,019	$ 5,647
Provision for warranty claims	9,667	6,994	6,127
Warranty claims paid	(7,775)	(6,500)	(6,809)
Exchange rate impact	23	8	54
Balance, end of the year	$ 7,436	$ 5,521	$ 5,019

In June 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 143 (Statement 143), Accounting for Asset Retirement Obligations . The Statement requires legal obligations associated with the retirement of long-lived assets to be recognized at their fair value at the time that the obligations are incurred. Upon initial recognition of a liability, that cost should be capitalized as part of the related long-lived asset and allocated to expense over the useful life of the asset. The Company adopted Statement 143 on January 1, 2003 and recorded an asset retirement obligation of $390,000 related to the removal of leasehold improvements that have been made to one of the Company s manufacturing and distribution centers. Such improvements must be removed upon termination of the lease agreement. As of December 31, 2006, the fair value of that obligation is $490,000.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

As of December 31, 2006, we employed a total of 4,224 people, consisting of 2,930 hourly and 1,294 salaried employees. Approximately 14.2% of the employees are represented by unions. The Grand Rapids, Michigan plant is the only unionized plant within the U.S and has an agreement with the Carpenters Union, Local 1615, of the United Brotherhood of Carpenters and Joiners of America, Affiliate of the Carpenters Industrial Council (the Union), covering approximately 418 hourly employees. The previous agreement was effective through August 27, 2006. On August 25, 2006, the Company entered into a new five-year collective bargaining agreement with the Union covering bargaining unit members at the Grand Rapids, Michigan facility. The Collective Bargaining Agreement was ratified on August 25, 2006 and became binding at that time. The Collective Bargaining Agreement sets forth the terms and conditions of employment for bargaining unit members working at the Company s Grand Rapids, Michigan facility and became effective on August 27, 2006, upon expiration of the previous agreement. The Collective Bargaining Agreement continues until August 27, 2011. Certain workers in the facilities in Italy are also represented by unions.

12. INCOME TAXES

Income before income tax expense consists of the following:

	2006	2005	2004
		(in thousands)	
U.S. operations	$ 75,876	$ 56,109	$ 43,748
Foreign operations	18,088	7,691	2,789
	$ 93,964	$ 63,800	$ 46,537

Income tax expense is comprised of the following:

	2006	2005	2004
		(in thousands)	
Current:			
Federal	$ 24,921	$ 16,550	$ 10,141
State	4,782	4,101	2,399
Foreign	6,930	4,313	1,221
Total current	36,633	24,964	13,761
Deferred:			
Federal	(875)	2,694	4,651
State	(188)	151	956
Foreign	(239)	82	425
Total deferred	(1,302)	2,927	6,032
Income tax expense	$ 35,331	$ 27,891	$ 19,793

Income taxes paid, net of refunds received, by the Company during 2006, 2005, and 2004 totaled $19,565,000, $6,624,000, and $6,407,000, respectively.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table sets forth the tax effects of temporary differences that give rise to the deferred tax assets and liabilities:

	2006	2005
	(in thousands)	
Deferred tax assets:		
Accounts receivable, principally due to allowance for doubtful accounts	$ 1,330	$ 1,267
Inventories	2,142	1,440
Net operating loss carryforwards	17,857	16,666
Accrued pension	12,959	7,582
Stock-based compensation	3,393	1,664
Compensation-related accruals	4,632	4,408
Warranty	2,738	2,045
Obligation for postretirement benefits other than pension	11,171	9,958
Accrued liabilities and other items	5,155	3,688
Gross deferred tax assets	61,377	48,718
Valuation allowance	(17,879)	(16,841)
Net deferred tax assets	43,498	31,877
Deferred tax liabilities:		
Intangibles, principally due to differences in amortization	54,326	48,056
Plant and equipment, principally due to differences in depreciation and assigned values	17,421	18,747
Gross deferred tax liabilities	71,747	66,803
Net deferred tax liabilities	$ (28,249)	$ (34,926)

As of December 31, 2006, the Company had net operating loss carryforwards totaling approximately $53,279,000 in various foreign tax jurisdictions, of which $253,000 expires in 2007, $252,000 in 2008, $1,192,000 in 2009, $940,000 in 2010, $836,000 in 2011, $1,068,000 in 2012, $426,000 in 2013, and $48,311,000 may be carried forward for an unlimited time.

Future tax benefits recognized through reductions of the valuation allowance for net operating loss carryforwards that existed as of February 29, 1996, the date the Company was formed, will generally reduce goodwill. The Company provides a valuation allowance against net foreign deferred tax assets due to the uncertainty that they can be realized.

The following table sets forth a reconciliation of the statutory federal income tax rate to the effective income tax rate:

	2006	2005	2004
Federal statutory tax rate	35.0%	35.0%	35.0%
Increase in the tax rate resulting from:			
State taxes, net of federal effect	3.2	3.5	5.1
Effect of tax rates of other countries		0.5	0.3
Non-deductible IPO expense	0.4		2.2
Taxes related to the repatriation of foreign earnings		4.9	

Other	(1.0)	(0.2)	(0.1)
Effective tax rate	37.6%	43.7%	42.5%

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company has not made provisions for U.S. federal and state income taxes as of December 31, 2006 on $72,375,000 of foreign earnings that are expected to be reinvested indefinitely. Upon distribution of those earnings in the form of dividends or otherwise, the Company would be subject to U.S. federal and state income taxes (subject to an adjustment for foreign tax credits) and withholding taxes payable to the various foreign countries. Determination of the amount of the unrecognized deferred tax liability is not practicable.

In the fourth quarter of 2004, the United States Congress passed The American Jobs Creation Act of 2004 (the Act), which introduced a new tax deduction for computing taxable profits from the sale of products manufactured in the United States and a special one-time dividends received deduction on the repatriation of certain foreign earnings upon meeting certain criteria. The Act provides for a deduction of 85% of foreign earnings that are repatriated. The deduction was available through December 31, 2005. On July 27, 2005, the Company formalized a plan to repatriate $45 million of foreign earnings from its Canadian operations. The Company repatriated $20 million during the third quarter of 2005 and repatriated the remaining $25 million during the fourth quarter of 2005. As a result of the repatriation, the Company recorded additional tax expense of $3.1 million in 2005.

13. LEASES

The Company has commitments under operating leases for certain machinery and equipment as well as manufacturing, warehousing, showroom and other facilities used in its operations. Some of the leases contain renewal provisions and generally require the Company to pay certain operating expenses, including utilities, insurance and taxes, which are subject to escalation. In 2004, the Company entered into a lease for one of its showrooms which contained a provision for cash abatements related to certain leasehold improvements. This abatement is recognized on a straight-line basis as a reduction to rent expense over the least term. The unamortized portion as of December 31, 2006 and 2005 was $1,586,000 and $1,826,000, respectively. Total rental expense for 2006, 2005, and 2004 was $12,035,000, $10,965,000 and $9,934,000, respectively. Future minimum rental payments required under those operating leases that have an initial or remaining noncancelable lease term in excess of one year are as follows (in thousands):

2007	$ 10,213
2008	9,655
2009	7,434
2010	5,769
2011	4,539
Subsequent years	7,816
Total minimum rental payments	$ 45,426

14. PENSION AND OTHER POSTRETIREMENT BENEFITS

The Company has two domestic defined benefit pension plans and two plans providing for other postretirement benefits, including medical and life insurance coverage. One of the pension plans and one of the other postretirement benefits plans cover eligible U.S. nonunion employees while the other pension plan and other postretirement benefits plan cover eligible U.S. union employees.

On December 31, 2006, the Company adopted the recognition and disclosure provisions of Statement 158. Statement 158 required the Company to recognize the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of its pension plan in the December 31, 2006 statement of financial position, with a corresponding adjustment to accumulated other comprehensive income, net of tax. The

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

adjustment to accumulated other comprehensive income at adoption represents the net unrecognized actuarial losses, unrecognized prior service costs, and unrecognized transition obligation remaining from the initial adoption of Statement 87, all of which were previously netted against the plan s funded status in the Company s statement of financial position pursuant to the provisions of Statement 87. These amounts will be subsequently recognized as net periodic pension cost pursuant to the Company s historical accounting policy for amortizing such amounts. Further, actuarial gains and losses that arise in subsequent periods and are not recognized as net periodic pensions cost in the same periods will be recognized as a component of net periodic pension cost on the same basis as the amounts recognized in accumulated other comprehensive income at adoption of Statement 158.

The following table sets forth a reconciliation of the benefit obligation, plan assets and accrued benefit cost related to the pension and other postretirement benefits provided by the Company (in thousands):

	Pension Benefits		Other Benefits	
	2006	2005	2006	2005
Change in projected benefit obligation:				
Projected benefit obligation at January 1	$ 107,995	$ 84,216	$ 27,018	$ 30,513
Service cost	9,666	8,629	634	876
Interest cost	6,346	5,240	1,564	1,866
Participant contributions	259	242		
Plan amendments			82	(12,479)
Actuarial (gain) loss	(1,395)	10,597	586	7,642
Benefits paid	(1,236)	(929)	(1,565)	(1,400)
Projected benefit obligation at December 31	$ 121,635	$ 107,995	$ 28,319	$ 27,018
Accumulated benefit obligation, December 31, 2006	$ 107,258	$ 95,414	$	$
Change in plan assets:				
Fair value of plan assets at January 1	$ 75,640	$ 58,331	$	$
Actual return on plan assets	6,798	6,970		
Employer contributions	6,914	11,026	1,565	1,400
Participant contributions	259	242		
Benefits paid	(1,236)	(929)	(1,565)	(1,400)
Fair value of plan assets at December 31	$ 88,375	$ 75,640	$	$
Funded status	$ (33,260)	$ (32,355)	$ (28,319)	$ (27,018)
Unrecognized net loss		19,846		16,486
Unrecognized prior service cost (benefit)		552		(14,712)
Net amount recognized		$ (11,957)		$ (25,244)

Effective January 1, 2006, the Company amended its post-65 retiree Health Care Plan to replace prescription drug coverage with a Medicare Part D reimbursement capped at $40 per month.

Effective January 1, 2007, the Company amended its post retirement Health Care Plan to share costs equally for retirees with 90 points (age plus years of service). Retirees with less than 90 points will pay the full cost of insurance.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following disclosures are required with the adoption of SFAS No. 158, Employers Accounting for Defined Benefit Pension and *Other Postretirement Plans* (in thousands):

	Pension Benefits		Other Benefits	
	2006	2005	2006	2005
Amounts recognized in the consolidated balance sheet consist of:				
Noncurrent assets	$	$	$	$
Current Liabilities	(5,813)	(3,039)	(1,684)	(1,380)
Noncurrent liabilities	(27,447)	(16,735)	(26,635)	(23,864)
Intangible Asset		552		
Accumulated other comprehensive income		7,265		
Net amount recognized	$ (33,260)	$ (11,957)	$ (28,319)	$ (25,244)
Amounts recognized in accumulated other comprehensive income:				
before taxes:				
Net actuarial loss (gain)	$ 16,937	$	$ 16,135	$
Prior service cost (benefit)	475		(13,275)	
Net amount recognized	$ 17,412	$	$ 2,860	$

The estimated net actuarial loss, and prior service cost, for the defined benefit pension plans included in accumulated other comprehensive income and expected to be recognized in net periodic pension cost during the fiscal year ended December 31, 2007 is $694,000, and $77,000, respectively.

The incremental effects of adopting the provisions of Statement 158 on the Company s statement of financial position at December 31, 2006 are presented in the following table. The adoption of Statement 158 had no effect on the Company s consolidated statement of income for the year ended December 31, 2006, or for any prior period presented, and it will not effect the Company s operating results in future periods. Had the Company not been required to adopt Statement 158 at December 31, 2006, it would have recognized an additional minimum pension liability pursuant to the provisions of Statement 87. The effect of recognizing the additional minimum liability is included in table below in the column labeled Prior to Application of Statement 158.

	December 31, 2006		
	Before Application of Statement 158	Effect of Adopting Statement 158 (in thousands)	After Application of Statement 158
Intangible asset (pension)	$ 475	$ (475)	$
Accrued pension liability	18,883	14,377	33,260
Postretirement benefits other than pensions liabilities	25,459	2,860	28,319
Accumulated other comprehensive income (net of taxes)	1,550	10,725	12,275
Deferred income taxes	1,009	6,988	7,997

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Weighted-average assumptions used to determine benefit obligations of the Company s pension and other postretirement benefit plans as of December 31, 2006 and 2005, are as follows:

	2006	2005
Discount rate	6.00%	5.90%
Rate of compensation increase	4.00	4.00

The following table sets forth the components of the net periodic benefit cost for the Company s pension and other postretirement benefits plans:

	Pension Benefits			Other Benefits		
	2006	2005	2004	2006	2005	2004
			(in thousands)			
Service cost	$ 9,666	$ 8,629	$ 8,990	$ 634	$ 875	$ 871
Interest cost	6,346	5,240	4,550	1,564	1,866	1,619
Expected return on plan assets	(6,225)	(4,902)	(4,166)			
Amortization of prior service cost	77	77	77	(1,354)	(223)	(223)
Recognized actuarial loss	942	180	356	937	433	269
Net periodic benefit cost	$ 10,806	$ 9,224	$ 9,807	$ 1,781	$ 2,951	$ 2,536
Additional Information						
Increase (decrease) in minimum liability included in other comprehensive income	$ (4,705)	$ 7,254	$ (4,072)	$	$	$

Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31, 2006 and 2005, are as follows:

	Pension Benefits		Other Benefits	
	2006	2005	2006	2005
Discount rate	5.90%	6.25%	5.90%	6.25%
Expected return on plan assets	8.50	8.50	N/A	N/A
Rate of compensation increase	4.00	4.00	4.00	4.00

The expected long-term rate of return on assets is based on management s expectations of long-term average rates of return to be earned on the investment portfolio. In establishing this assumption, management considers historical and expected returns for the asset classes in which the plan assets are invested.

For purposes of measuring the benefit obligation as of and for the year ended December 31, 2006, associated with the Company s other postretirement benefit plans, a 9% annual rate of increase in the per capital cost of covered health care benefits was assumed for 2007. The rate was then assumed to decrease 1.0% per year to an ultimate rate of 5% for 2011 and thereafter. For purpose of measuring the net periodic benefit cost as of and for the year ended December 31, 2006 associated with the Company s other postretirement benefits plans, a 7.0% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2006. Increasing the assumed health care cost trend rate by 1.0% would increase the benefit obligation as of December 31, 2006 by $4,213,000 and increase the aggregate of the service and interest cost components of net periodic benefit cost for 2006 by $253,000. Decreasing the assumed health care cost trend rate by 1.0% would decrease the benefit

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

obligation as of December 31, 2006 by $3,352,000 and decrease the aggregate of the service and interest cost components of net periodic benefit cost for 2006 by $201,000.

The Company s pension plans weighted-average asset allocations as of December 31, 2006 and 2005, by asset category are as follows:

Asset Category	Plan Assets at December 31 2006	2005
Temporary Investment Funds	4%	1%
Equity Investment Funds	62	65
Fixed Income Funds	34	34
Total	100%	100%

The Company s pension plans investment policy includes an asset mix based on the Company s risk posture. The investment policy states a target allocation of 60% equity funds and 40% fixed income funds. Inclusion of the fixed income funds is to provide growth through income and these funds should primarily invest in fixed income instruments of the U.S. Treasury and government agencies and investment-grade corporate bonds. The equity fund investments can consist of a broadly diversified domestic equity fund, an actively managed domestic equity fund and an actively managed international equity fund. The purpose of these funds is to provide the opportunity for capital appreciation, income, and the ability to diversify investments outside the U.S. equity market. Mutual funds are used as the plans investment vehicle since they have clearly stated investment objectives and guidelines, offer a high degree of investment flexibility, offer competitive long-term results, and are cost effective for small asset balances.

The Company expects to contribute $5,813,000 to its pension plans and $1,684,000 to its other postretirement benefit plans in 2007. Estimated future benefit payments under our pension and other postretirement plans are as follows:

	Pension Benefits (in thousands)	Other Benefits
2007	$ 1,726	$ 1,684
2008	2,162	1,747
2009	2,686	1,716
2010	3,331	1,966
2011	4,092	2,153
2012-2016	35,754	11,376

Employees of the Canadian, Belgium and United Kingdom operations participate in defined contribution pension plans sponsored by the Company. The Company s expense related to these plans for 2006, 2005, and 2004 was $1,352,000, $1,105,000, and $937,000 respectively.

The Company also sponsors a 401(k) retirement savings plan for all U.S. employees. Under this plan, participants may defer a portion of their earnings up to the annual contribution limits established by the Internal Revenue Service. The Company matches 40.0% of participant contributions up to the first 6.0% of compensation for nonunion employees and matches 50.0% of participant contributions up to the first 6.0% of compensation for union employees. For participants who are nonunion employees, the plan provides for additional discretionary employer matching based on the achievement of certain profitability goals. The plan also provides that the Company may make discretionary contributions of common stock to participant accounts on behalf of all

KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

actively employed U.S. participants. Contributed shares of common stock are restricted from transfer or withdrawal while participants remain employed. However, upon retirement, death or termination of employment, a participant s balance of contributed shares of common stock may be transferred to another fund or distributed at the participant s discretion, and any shares that are not vested at such time are forfeited by the participant and held by the plan. Company contributions generally vest ratably over a five-year period. A Knoll common stock fund consisting of 1,000,000 shares of common stock into which participants may invest the compensation they elect to defer was established on December 14, 2004. Participant contributions into the Knoll common stock fund will be limited to no more than 10% of their total account balance in the plan. Participant contributions in the Knoll common stock fund may be transferred into other investment alternatives and distributed in the form of shares of Knoll common stock if so invested at the time of distribution.

The Company s total expense under the 401(k) plan was $2,802,000, $3,035,000, and $2,915,000 for 2006, 2005 and 2004, respectively.

15. STOCK PLANS

Stock Incentive Plans

The Company sponsors two stock incentive plans under which awards denominated or payable in shares or options to purchase shares of Knoll common stock may be granted to officers, certain other key employees, directors and consultants of the Company. On February 28, 2006, one of the Company s three stock incentive plans expired reducing the number of shares available to grant under the plans by approximately 447,000. As of December 31, 2006, a combined maximum of 23,978,858 shares were authorized for issuance under the plans. A Stock Option Committee currently consisting of the Company s entire Board of Directors (Stock Option Committee) has sole discretion concerning administration of the plans, including selection of individuals to receive awards, types of awards, the terms and conditions of the awards and the time at which awards will be granted. Options that are granted have a maximum contractual life of ten years. Grants to employees generally become partially vested one year from the date of the award agreement. On such date for the majority of options granted, 30% of the shares covered by the options become available for exercise. An additional 20% vest and become available on the second and third anniversaries and an additional 30% on the fourth anniversary. For some of the options granted 25% vest each year for four years. In addition, the options generally have accelerated vesting provisions upon a change of control of the Company. With the implementation of SFAS 123(R), the Company is recognizing compensation expense using the graded vesting attribution method which treats each option grant as multiple grants each with its own requisite service period.

Under the Amended and Restated 1999 Stock Incentive Plan, the Company has granted performance-based restricted stock awards to certain key employees aggregating 1,650,000 shares of common stock. These awards provide for the delivery of shares of common stock to award recipients upon the satisfaction of certain vesting requirements. The restricted stock awards will vest as to one-sixth of the shares underlying each award to the extent that the average Knoll operating profit for any two-year period is equal to $100.0 million. An additional one-sixth will vest based on additional increments to operating profit of $15.0 million over such a period, with full vesting upon the achievement of $175.0 million in average operating profit over such a period. In any event, the awards will fully vest on the sixth anniversary of the date of the grant and will be subject to pro rata vesting upon a change of control of the Company, if earlier, regardless of whether the operating profit targets are met. The Company determined the fair value of the shares on the date of grant and is recognizing compensation expense ratably over the vesting period.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table summarizes the Company s restricted stock activity during the year:

	2006	
	Number of Shares Granted	Weighted Average Fair Value
Outstanding at the beginning of the year	1,650,000	$ 15.11
Granted		
Forfeited	(64,000)	15.00
Outstanding at the end of the year	1,586,000	15.11

The following table summarizes the Company s stock option activity during the year:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Balance at December 31, 2005	7,611,245	$ 11.39		
Exercised	(2,808,812)	10.14		
Granted	25,000	20.04		
Expired				
Forfeited	(52,887)	14.52		
Balance at December 31, 2006	4,774,546	$ 13.64	4.87	$ 39,915
Exercisable at end of year	3,825,925	$ 13.14	4.12	$ 33,898

Generally, options were granted with an exercise price that equals the market price of a share of Knoll common stock on the date of grant, while the Company s stock was publicly traded, or the estimated fair value of a share of Knoll common stock on the date of grant, using an outside appraisal, subsequent to November 4, 1999 through December 13, 2004, when the Company s stock was not publicly traded. Options that were granted generally vest in installments over either a four- or five-year period, beginning one year from the date of grant.

The following table summarizes information regarding stock options outstanding and exercisable at December 31, 2006:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number of Options	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price

$6.12-$10.94	2,016,919	2.85 years	$ 10.65	2,016,919	$ 10.65
$14.52-$20.04	2,757,627	6.36	15.83	1,809,006	15.92
$6.12-$20.04	4,774,546	4.87	13.64	3,825,925	13.14

The weighted-average grant-date fair value of options granted during the years 2006, 2005, and 2004 was $5.27, $3.80 and $4.07 respectively. The total intrinsic value of options exercised during the years 2006, 2005,

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

and 2004 was $26.9 million, $21.2 million, and $13.8 million, respectively. The total fair value of shares vested during the years 2006, 2005, and 2004 was $5.0 million, $4.9 million, and $5.5 million, respectively.

A summary of the status of the Company s non-vested shares as of December 31, 2006, and changes during the year ended December 31, 2006, is presented below.

	Number of Options	Weighted Average Grant-Date Fair Value
Nonvested at January 1, 2006	1,680,061	4.26
Granted	25,000	5.27
Vested	(703,553)	5.10
Forfeited	(52,887)	3.81
Nonvested at December 31, 2006	948,621	3.81

As of December 31, 2006, there was $16.6 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the plans. That cost is expected to be recognized over a weighted-average period of 3.9 years.

Other Stock-Based Compensation Plans

On November 4, 1999, the Company established The Knoll Stock Ownership Award Plan, under which it may grant notional stock units to substantially all individuals employed by the Company in Canada as of the effective date of the plan. Participants vest their interest in notional stock units ratably according to years of service, with such units being 100% vested at the end of five years of service. On November 4, 1999, the Company granted a total of 109,800 notional stock units, with an estimated fair value of $14.00 per unit, to eligible employees. All outstanding shares became fully vested on November 4, 2004. In September 2004 and in January 2001, the number of notional units outstanding was adjusted, in accordance with the plan provisions, in response to special cash dividends that were paid to stockholders. In addition the number of notional units outstanding was adjusted, in accordance with plan provisions, for each quarterly cash dividend declared since the Company went public December 14, 2004. Compensation expense is recognized based on the estimated fair value of notional stock units and vesting provisions. Total compensation expense (income) incurred in connection with this award was $1,972,000 for 2006, $612,000 for 2005 and $747,000 for 2004. Units forfeited totaled 102 in 2004.

As of December 31, 2006, approximately 119,139 notional units were outstanding and fully vested.

As discussed in Note 14, the Company may contribute shares of Knoll common stock into participant 401(k) plan accounts at its discretion. The Company contributed 300,200 shares into the 401(k) plan for substantially all individuals employed by the Company in the U.S. as of November 4, 1999. In connection with this award, the Company recognized $4,203,000 of compensation expense, which was based on a value of $14.00 per share. During 2006, 2005, and 2004 the Company repurchased 7,200, 7,300, and 13,200 of the contributed common shares, respectively, from the 401(k) plan at a weighted average price per share of $19.51 during 2006, $16.89 during 2005, and $16.67 during 2004, respectively. Such shares are held in treasury.

In December 2004, the Company established an Employee Stock Purchase Plan (ESPP) whereby employees of the Company may purchase shares of Knoll Inc. at a discounted rate. The discount rate is 5% off the average of the high and low sale price per share on the last Trading Day of the purchase period. Employees may

KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

contribute 1-10% of their eligible gross pay up to a $25,000 annual stock value limit. In 2006 and 2005, employees purchased 3,433 and 3,953 shares, respectively in accordance with the terms of the ESPP.

16. SEGMENT AND GEOGRAPHIC REGION INFORMATION

In accordance with Statement of Financial Accounting Standards No. 131, Disclosures about Segments of an Enterprise and Related Information, management evaluates the Company as one reporting segment in the office furniture industry. The Company is engaged worldwide in the design, manufacture and sale of office furniture products and accessories through its wholly owned subsidiaries. Throughout the world, the product offerings, the production processes, the methods of distribution, and the customers serviced are similar. The Company s product offerings consist primarily of office furniture systems, seating, files and storage, and other specialty products. These product offerings are marketed, distributed, and managed primarily as a group of similar products on an overall portfolio basis.

The Company s net sales by product category are as follows:

	Year Ended December 31,		
	2006	2005 (in thousands)	2004
Office Systems	$ 555,006	$ 458,840	$ 402,313
Specialty Products	158,792	134,372	116,570
Seating	105,149	84,417	69,038
Files and Storage	81,314	58,750	51,616
European Products	76,381	63,017	54,411
Other	5,510	8,564	12,442
	$ 982,152	$ 807,960	$ 706,390

The Company markets its products in the United States and internationally, with its principal international markets being Canada and Europe. The table below contains information about the geographical areas in which the Company operates. Sales to clients are attributed to the geographic areas based on the origin of sale.

	United States	Canada	Europe	Consolidated
		(in thousands)		
2006				
Sales to clients	$ 870,713	$ 33,216	$ 78,223	$ 982,152
Property, plant and equipment, net	88,105	35,513	14,111	137,729
2005				
Sales to clients	$ 715,453	$ 29,490	$ 63,017	$ 807,960
Property, plant and equipment, net	95,074	35,070	12,022	142,166
2004				
Sales to clients	$ 633,787	$ 18,192	$ 54,411	$ 706,390
Property, plant and equipment, net	103,225	33,722	14,045	150,992

A number of U.S. government agencies purchase the Company s products through multiple contracts with the General Services Administration (GSA). Sales under GSA contracts amounted to $124,183,000 in 2006, $99,291,000 in 2005, and $120,495,000 in 2004.

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KNOLL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

17. QUARTERLY RESULTS (UNAUDITED)

The following tables contain selected unaudited Consolidated Statements of Operations data for each quarter for the years ended December 31, 2006 and 2005. The operating results for any quarter are not necessarily indicative of results for any future period.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Fiscal Year
		(in thousands, except per share data)			
2006					
Sales	$ 218,100	$ 247,476	$ 243,609	$ 272,967	$ 982,152
Gross profit	69,773	78,965	81,220	89,079	319,037
Net income	10,253	14,752	15,639	17,989	58,633
Earnings per share basic	$ .19	$ .29	$ .32	$ .38	$ 1.18
Earnings per share diluted	$ .19	$ .28	$ .31	$ .37	$ 1.14
2005					
Sales	$ 179,129	$ 197,726	$ 209,333	$ 221,772	$ 807,960
Gross profit	58,089	68,187	71,433	74,347	272,056
Net income	6,851	11,368	8,196	9,494	35,909
Earnings per share basic	$ .14	$ .22	$ .16	$ .18	$ .70
Earnings per share diluted	$ .13	$ .22	$ .15	$ .18	$ .68

18. OTHER (EXPENSE) INCOME

The components of other (expense) income are as follows:

	December 31 2006	2005	2004
		(in thousands)	
Foreign exchange transaction gain (loss)	$ 562	$ (2,261)	$ (3,427)
Unrealized (loss) gain on derivatives	(703)	295	695
Write-off of deferred financing fees		(3,562)	(2,518)
Fees associated with the amended and restated credit agreement		(1,056)	
Other	882	1,229	(66)
Other income (expense), net	$ 741	$ (5,355)	$ (5,316)

KNOLL, INC.

Report of Independent Registered Public Accounting Firm

on Consolidated Financial Statements and Schedule

The Board of Directors and Stockholders

Knoll, Inc.

We have audited the accompanying consolidated balance sheets of Knoll, Inc. as of December 31, 2006 and 2005, and the related consolidated statements of operations, stockholders equity (deficit), and cash flows for each of the three years in the period ended December 31, 2006. Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Knoll, Inc. at December 31, 2006 and 2005, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in Note 2 to the consolidated financial statements, the Company changed its method for Accounting for employee stock compensation plans and defined benefit pension and other postretirement plans in 2006.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Knoll, Inc. s internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 9, 2007, expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Philadelphia, Pennsylvania

March 9, 2007

Item 9. ***Changes In And Disagreements With Accountants On Accounting And Financial Disclosures***

None

Item 9A. ***Controls And Procedures***

Evaluation of disclosure controls and procedures. Our Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report, pursuant to Rule 13(a)-15(e) under the Securities Exchange Act of 1934, as amended, and concluded that our disclosure controls and procedures were effective.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Management s annual report on internal control over financial reporting. Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended, for the Company. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control over financial reporting includes without limitation, maintaining records that in reasonable detail accurately and fairly reflect our transactions, providing reasonable assurance that transactions are recorded as necessary for preparation of our financial statements, providing reasonable assurance that receipts and expenditures of company assets are made in accordance with management authorization, and providing reasonable assurance that unauthorized acquisition, use or disposition of company assets that could have a material effect on our financial statements would be prevented or detected on a timely basis. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

Our management assessed the effectiveness of our internal control over financial reporting based on the framework in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management concluded that the Company s internal control over financial reporting was effective as of December 31, 2006. Our independent registered public accounting firm, Ernst & Young LLP, has audited our management s assessment of the effectiveness of our internal control over financial reporting as of December 31, 2006; their report is included on page 60.

No change in our internal control over financial reporting occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended.

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Report of Independent Registered Public Accounting Firm

on Internal Control Over Financial Reporting

The Board of Directors and Stockholders

Knoll, Inc.

We have audited management s assessment, included in the accompanying Report of Management on Internal Control Over Financial Reporting, that Knoll, Inc. maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Knoll, Inc. s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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

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

In our opinion, management s assessment that Knoll, Inc. maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Knoll, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the COSO criteria**.**

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the 2006 consolidated financial statements of Knoll Inc. and our report dated March 9, 2007, expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Philadelphia, Pennsylvania

March 9, 2007

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Item 9B. ***Other Information***

None.

PART III

Item 10. ***Directors, Executive Officers And Corporate Governance***

The information relating to directors and director nominees of the registrant is incorporated by reference in our Proxy Statement for our 2007 Annual Meeting of Stockholders (the Proxy Statement).

The information relating to the identification of the audit committee, audit committee financial expert and director nomination procedures of the registrant is incorporated by reference in our Proxy Statement.

Our Board of Directors has adopted a code of ethics for all employees. This code is made available free of charge on our website at www.knoll.com. For further information see subsection Code of Ethics in our Proxy Statement.

Item 11. ***Executive Compensation***

The information required by Item 11 is hereby incorporated by reference in our Proxy Statement.

Item 12. ***Security Ownership Of Certain Beneficial Owners And Management And Related Stockholder Matters***

Securities Authorized for Issuance Under Equity Compensation Plans

Equity Compensation Plan Information
As of December 31, 2006

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options (a)	Weighted-Average Exercise Price of Outstanding Options (b)	Number of Shares Remaining for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a)) (c)
Equity compensation plans approved by security holders	4,774,546	$13.64	1,273,794
Equity compensation plans not approved by security holders			
Total	4,774,546		1,273,794

If there is an expiration, termination, or cancellation of any benefit granted under the plans without the issuance of shares, the shares subject to or reserved for that benefit may again be used for new stock options, rights, or awards of any type authorized under the plans.

All other information required by Item 12 is hereby incorporated by reference in our Proxy Statement.

Item 13. ***Certain Relationships And Related Transactions, And Director Independence***

The information required by Item 13 is hereby incorporated by reference in our Proxy Statement.

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Item 14. ***Principal Accounting Fees And Services***

The information required by Item 14 is hereby incorporated by reference in our Proxy Statement.

PART IV

Item 15. ***Exhibits And Financial Statement Schedules***

(a) Documents filed as part of this Form 10-K:

(1) CONSOLIDATED FINANCIAL STATEMENTS (ITEM 8)

Consolidated Balance Sheets as of December 31, 2006 and 2005.

Consolidated Statements of Operations for the Years Ended December 31, 2006, 2005, and 2004.

Consolidated Statements of Stockholders Equity (Deficit) for the Years Ended December 31, 2006, 2005, and 2004.

Consolidated Statements of Cash Flows for the Years Ended December 31, 2006, 2005, and 2004.

Notes to the Consolidated Financial Statements.

Report of Independent Registered Public Accounting Firm on Consolidated Financial Statements and Schedule.

(2) FINANCIAL STATEMENT SCHEDULES

Financial Statement Schedule II Valuation and Qualifying Accounts is filed with this Form 10-K on page S-1 of this Form 10-K. All other schedules for which provision is made in the applicable regulation of the Commission are not required under the related instructions or are inapplicable and therefore have been omitted.

(3) EXHIBITS

Exhibit Number	Description
3.1(a)	Amended and Restated Certificate of Incorporation of Knoll, Inc.
3.2(a)	Amended and Restated By-Laws of Knoll, Inc.
4.1(a)	Form of Stock Certificate.
10.1(b)	Stock Purchase Agreement, dated as of December 20, 1995, by and between Westinghouse and T.K.G. Acquisition Corp.
10.2(c)	Amended and Restated Credit Agreement, dated as of October 3, 2005, by and among Knoll, Inc., the Lenders (as defined therein), Bank of America, N.A., as Administrative Agent, UBS Securities LLC, as Syndication Agent, UBS Securities LLC and Banc of America Securities LLC, as Joint Lead Arrangers and Joint Bookrunners, Citibank, F.S.B., Manufacturers and Trades Trust Company and Harris, N.A., as Co-Documentation Agents.

10.3(k)	Incremental term loan assumption agreement, dated August 1, 2006, between Knoll, Inc. and Bank of America, N.A.
10.4(k)	Incremental revolving loan assumption agreement, dated August 1, 2006, between Knoll, Inc. and Bank of America, N.A.
10.5(d)*	Amended and Restated Employment Agreement, dated as of January 1, 2000, between Knoll, Inc. and Burton B. Staniar.
10.6(f)*	Amendment to Employment Agreement, dated as of March 25, 2002, between Knoll, Inc. and Burton B. Staniar.

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Exhibit Number	Description
10.7(j)*	Amended and Restated Employment Agreement, executed March 14, 2006, effective as of January 1, 2006, between Knoll, Inc and Burton B. Staniar.
10.8(e)*	Employment Agreement, dated as of March 23, 2001, between Knoll, Inc. and Andrew B. Cogan.
10.9(a)*	Amendment No. 1 to Amended and Restated Employment Agreement, dated as of August 25, 2004, between Knoll, Inc. and Andrew B. Cogan.
10.10(j)*	Amendment No. 2 to Employment Agreement, dated as of March 14, 2006, between Knoll, Inc. and Andrew B. Cogan.
10.11(l) *	Amendment No. 3 to Employment Agreement, dated as of December 11, 2006, between Knoll, Inc. and Andrew B. Cogan.
10.12(e)*	Employment Agreement, dated as of March 23, 2001, between Knoll, Inc. and Kathleen G. Bradley.
10.13(a)*	Amendment No. 1 to Amended and Restated Employment Agreement, dated as of August 25, 2004, between Knoll, Inc. and Kathleen G. Bradley.
10.14(j)*	Amendment No. 2 to Employment Agreement, dated as of March 14, 2006, between Knoll, Inc. and Kathleen G. Bradley.
10.15(l) *	Amendment No. 3 to Employment Agreement, dated as of December 11, 2006, between Knoll, Inc. and Kathleen G. Bradley.
10.16*	Summary of Barry L. McCabe 2007 Compensation.
10.17(a)*	Offer Letter, dated March 11, 1999, from Knoll, Inc. to Stephen A. Grover.
10.18*	Summary of Stephen A. Grover 2007 Compensation.
10.19(a)*	Offer Letter, dated July 30, 1999, from Knoll, Inc. to Arthur C. Graves.
10.20*	Summary of Arthur C. Graves 2007 Compensation.
10.21(d)	Amended and Restated Stockholders Agreement, dated as of November 4, 1999, among Knoll, Inc., Warburg, Pincus Ventures, L.P., and the signatories thereto.
10.22(a)	Amendment and Waiver to Amended and Restated Stockholders Agreement, dated as of October 1, 2004, among Knoll, Inc., Warburg, Pincus Ventures, L.P., and the signatories thereto.
10.23(d)	Amended and Restated Stockholders Agreement (Common Stock Under Stock Incentive Plans), dated as of November 4, 1999, among Knoll, Inc., Warburg, Pincus Ventures, L.P., and the signatories thereto.
10.24(a)	Amendment and Waiver to Amended and Restated Stockholders Agreement (Common Stock Under Stock Incentive Plans), dated as of September 8, 2004, among Knoll, Inc., Warburg, Pincus Ventures, L.P., and the signatories thereto.
10.25(d)*	Amended and Restated Knoll, Inc. 1996 Stock Incentive Plan.
10.26(d)*	Amended and Restated Knoll, Inc. 1997 Stock Incentive Plan.
10.27(a)*	Form of Amended and Restated Knoll, Inc. 1999 Stock Incentive Plan.
10.28(g)*	Form of Non-Qualified Stock Option Agreement under the Amended and Restated Knoll, Inc. 1996 Stock Incentive Plan, entered into by Knoll, Inc. and certain executive officers.
10.29(g)*	Form of Non-Qualified Stock Option Agreement under the Amended and Restated Knoll, Inc. 1997 Stock Incentive Plan, entered into by Knoll, Inc. and certain executive officers.

Exhibit Number	Description
10.30(d)*	Form of Non-Qualified Stock Option Agreement under the Amended and Restated Knoll, Inc. 1999 Stock Incentive Plan, entered into by Knoll, Inc. and certain executive officers.
10.31(a)*	Form of Restricted Stock Agreement under the Amended and Restated Knoll, Inc. 1999 Stock Incentive Plan.
10.32(n)	Agreement between the Knoll, Inc. Grand Rapids and United Brotherhood of Carpenters and Joiners of America Carpenters Industrial Council Local 1615, dated August 27, 2006.
10.33(a)*	Form of Director and Officer Indemnification Agreement.
10.34(a)*	Offer Letter, dated October 6, 2004, from Knoll, Inc. to John F. Maypole.
10.35(a)*	Offer Letter, dated October 6, 2004, from Knoll, Inc. to Anthony P. Terracciano.
10.36(a)*	Form of Knoll Employee Stock Purchase Plan.
10.37(h)*	Offer Letter, dated November 23, 2005, from Knoll, Inc. to Stephen F. Fisher.
10.38(j)*	Summary of Informal Healthcare Severance Policy
10.39(j)*	Form of Amendment to Restricted Share Agreement under the Amended and Restated Knoll, Inc. 1999 Stock Incentive Plan.
10.40(j)*	Amendment to Restricted Share Agreement under the Knoll, Inc. 1999 Stock Incentive Plan, dated March 14, 2006, between Knoll, Inc. and Kathleen G. Bradley.
10.41(j)*	Amendment to Restricted Share Agreement under the Knoll, Inc. 1999 Stock Incentive Plan, dated March 14, 2006, between Knoll, Inc. and Andrew B. Cogan.
10.42(j)*	Amendment to Restricted Share Agreement under the Knoll, Inc. 1999 Stock Incentive Plan, dated March 14, 2006, between Knoll, Inc. and Burton B. Staniar.
10.43(j)*	Amendment to Restricted Share Agreement under the Knoll, Inc. 1999 Stock Incentive Plan, dated March 14, 2006, between Knoll, Inc. and Stephen A. Grover.
10.44(j)*	Amendment to Restricted Share Agreement under the Knoll, Inc. 1999 Stock Incentive Plan, dated March 14, 2006, between Knoll, Inc. and Arthur C. Graves.
10.45(j)*	Amendment to Restricted Share Agreement under the Knoll, Inc. 1999 Stock Incentive Plan, dated March 14, 2006, between Knoll, Inc. and Barry L. McCabe.
10.46(k)	Stock Purchase Agreement, dated August 1, 2006, between Knoll, Inc. and Warburg Pincus Ventures, L.P.
10.47(m)*	Offer Letter, dated September 25, 2006, from Knoll, Inc. to Sarah E. Nash.
10.48(l)*	Andrew B. Cogan Incentive Compensation Letter, dated December 5, 2006.
10.49(l)*	Kathleen G. Bradley Incentive Compensation Letter, dated December 5, 2006.
10.50(l)*	Barry L. McCabe Incentive Compensation Letter, dated December 5, 2006.
10.51(l)*	Stephen A. Grover Incentive Compensation Letter, dated December 5, 2006.
10.52(l)*	Arthur C. Graves Incentive Compensation Letter, dated December 5, 2006.
21(a)	Subsidiaries of Knoll, Inc.
23.1	Consent of Independent Registered Public Accounting Firm.
24.1	Power of Attorney [(included on signature page)]

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Exhibit Number	Description
31.1	Certification for Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification for Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
32.1	Certification for Chief Executive Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification for Chief Financial Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(a) Incorporated by reference to Knoll, Inc. s Registration Statement on Form S-1 (File No. 333-118901), which was declared effective by the Commission on December 13, 2004.
(b) Incorporated by reference to Knoll, Inc. s Registration Statement on Form S-4 (File No. 333-2972), which was declared effective by the Commission on June 12, 1996.
(c) Incorporated by reference to Knoll, Inc. s Current Report on Form 8-K, which was filed with the Commission on October 4, 2005.
(d) Incorporated by reference to Knoll, Inc. s Annual Report on Form 10-K for the year ended December 31, 1999.
(e) Incorporated by reference to Knoll, Inc. s Annual Report on Form 10-K for the year ended December 31, 2000.
(f) Incorporated by reference to Knoll, Inc. s Annual Report on Form 10-K for the year ended December 31, 2001.
(g) See Exhibit 10.24. Exhibit is substantially identical to Exhibit 10.24.
(h) Incorporated by reference to Knoll, Inc. s Annual Report on Form 10-K for the year ended December 31, 2002.
(i) Incorporated by reference to Knoll, Inc. s Current Report on Form 8-K filed with the Commission on December 6, 2005.
(j) Incorporated by reference to Knoll, Inc. s Annual Report on Form 10-K for the year ended December 31, 2005
(k) Incorporated by reference to Knoll, Inc. s Current Report on Form 8-K filed with the Commission on August 3, 2006
(l) Incorporated by reference to Knoll, Inc. s Current Report on Form 8-K filed with the Commission on December 11, 2006
(m) Incorporated by reference to Knoll, Inc. s Current Report on Form 8-K filed with the Commission on September 27, 2006
(n) Incorporated by reference to Knoll, Inc. s Current Report on Form 8-K filed with the Commission on August 28, 2006
* Management Contract or Compensatory Plan or Arrangement required to be identified by Item 15(a) (3) of Form 10-K.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, on this 16th day of March 2007.

KNOLL, INC.

By: /s/ ANDREW B. COGAN
Andrew B. Cogan

Chief Executive Officer

KNOW ALL PERSONS BY THESE PRESENTS, that each individual whose signature appears below constitutes and appoints Andrew B. Cogan and Barry L. McCabe, and each of them, his true and lawful attorneys-in-fact and agents with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this Form 10-K, and to file the same, with all exhibits thereto and all documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or his or their substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report on Form 10-K has been signed by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

/s/ BURTON B. STANIAR **Burton B. Staniar**	Chairman of the Board	March 16, 2007
/s/ ANDREW B. COGAN **Andrew B. Cogan**	Chief Executive Officer, Knoll, Inc. and Director	March 16, 2007
/s/ KATHLEEN G. BRADLEY **Kathleen G. Bradley**	President and Chief Executive Officer, Knoll North America and Director	March 16, 2007
/s/ BARRY L. MCCABE **Barry L. McCabe**	Chief Financial Officer	March 16, 2007
/s/ JEFFREY A. HARRIS **Jeffrey A. Harris**	Director	March 16, 2007
/s/ SIDNEY LAPIDUS **Sidney Lapidus**	Director	March 16, 2007
/s/ KEWSONG LEE **Kewsong Lee**	Director	March 16, 2007

/s/ JOHN F. MAYPOLE	Director	March 16, 2007
John F. Maypole		

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/s/ Anthony P. Terracciano **Anthony P. Terracciano**	Director	March 16, 2007
/s/ Sarah E. Nash **Sarah E. Nash**	Director	March 16, 2007
/s/ Stephen F. Fisher **Stephen F. Fisher**	Director	March 16, 2007

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SCHEDULE II

KNOLL, INC.

VALUATION AND QUALIFYING ACCOUNTS

(In Thousands)

Description	Balance at Beginning of Year	Additions Charged to Expenses	Charge-Offs	Other (1)	Balance at End of Year
Allowance for doubtful accounts:					
Year ended December 31, 2004	$ 5,488	$ 2,427	$ 2,582	$ 59	$ 5,392
Year ended December 31, 2005	5,392	1,321	2,796	(91)	3,826
Year ended December 31, 2006	3,826	1,224	1,660	(53)	3,337
Allowance for other non-trade receivables:					
Year ended December 31, 2004	1,980				1,980
Year ended December 31, 2005	1,980		329		1,651
Year ended December 31, 2006	1,651		274		1,377
Reserve for inventory valuation:					
Year ended December 31, 2004	6,559	1,197	1,654	245	6,347
Year ended December 31, 2005	6,347	971	2,026	(261)	5,031
Year ended December 31, 2006	5,031	2,239	982	174	6,462
Valuation allowance for deferred income tax assets:					
Year ended December 31, 2004	17,033	1,119	4,432	2,274	15,994
Year ended December 31, 2005	15,994	1,171	488	164	16,841
Year ended December 31, 2006	16,841	1,046	2,163	2,155	17,879
Reserve for warranty claims:					
Year ended December 31, 2004	5,647	6,127	6,809	54	5,019
Year ended December 31, 2005	5,019	6,994	6,500	8	5,521
Year ended December 31, 2006	5,521	9,667	7,775	23	7,436

(1) Primarily the impact of currency changes