

ARMSTRONG WORLD INDUSTRIES INC

FORM 10-K (Annual Report)

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Address	2500 COLUMBIA AVE LANCASTER, PA 17603
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Sector	Capital Goods
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FORM 10-K

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

(Mark One)

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

For the fiscal year ended December 31, 1997

OR

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

For the transition period from _____ to _____

Commission file number 1-2116

Armstrong World Industries, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania 23-0366390

(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

P. O. Box 3001, Lancaster, Pennsylvania 17604

(Address of principal executive offices) (Zip Code)

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

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

Title of each class -----	Name of each exchange on which registered -----
Common Stock (\$1 par value)	New York Stock Exchange, Inc.
Preferred Stock Purchase Rights	Pacific Stock Exchange, Inc. (a)
9-3/4% Debentures Due 2008	Philadelphia Stock Exchange, Inc. (a) (a) Common Stock and Preferred Stock Purchase Rights only

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

None

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

Yes 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]

The aggregate market value of the Common Stock of registrant held by non-affiliates of the registrant based on the closing price (\$72.8125 per share) on the New York Stock Exchange on February 10, 1998, was approximately \$2.7 billion. For the purposes of determining this amount only, registrant has defined affiliates as including (a) the executive officers named in Item 10 of this 10-K Report, (b) all directors of registrant, and (c) each shareholder that has informed registrant by February 14, 1998, as having sole or shared voting power over 5% or more of the outstanding Common Stock of registrant as of December 31, 1997. As of February 10, 1998, the number of shares outstanding of registrant's Common Stock was 40,076,306. This amount includes the 4,826,203 shares of Common Stock as of December 31, 1997, held by Mellon Bank, N.A., as Trustee for the employee stock ownership accounts of the Company's Retirement Savings and Stock Ownership Plan.

Documents Incorporated by Reference

Portions of the Proxy Statement dated March 16, 1998, relative to the April 27, 1998, annual meeting of the shareholders of registrant (the "Company's 1998 Proxy Statement") have been incorporated by reference into Part III of this Form 10-K Report.

PART I

Item 1. Business

Armstrong World Industries, Inc. is a Pennsylvania corporation incorporated in 1891. The Company is a manufacturer of interior furnishings, including floor coverings, and building products which are sold primarily for use in the furnishing, refurbishing, repair, modernization and construction of residential, commercial and institutional buildings. It also manufactures various industrial and other products. In late 1995, Armstrong sold its furniture business and combined its ceramic tile business with Dal-Tile International Inc. ("Dal-Tile"), retaining a minority equity interest in the combined company. Unless the context indicates otherwise, the term "Company" means Armstrong World Industries, Inc. and its consolidated subsidiaries.

Industry Segments

The company's businesses include four reportable segments: floor coverings, building products, industry products and ceramic tile.

NATURE OF OPERATIONS

at December 31 (millions)	1997	1996	1995
Net trade sales:			
Floor coverings	\$1,116.0	\$1,091.8	\$1,053.9
Building products	754.5	718.4	682.2
Industry products	328.2	346.2	348.8
Ceramic tile	--	--	240.1
Total net sales	\$2,198.7	\$2,156.4	\$2,325.0
Operating income (loss): (Note 1)			
Floor coverings	\$ 186.5	\$ 146.9	\$ 145.0
Building products	122.3	95.1	92.2
Industry products	55.5	40.1	9.3
Ceramic tile (Note 2)	(42.4)	9.9	(168.4)
Unallocated corporate expense	0.1	(36.1)	(34.0)
Total operating income	\$ 322.0	\$ 255.9	\$ 44.1
Depreciation and amortization:			
Floor coverings	\$ 65.5	\$ 53.9	\$ 47.9
Building products	37.5	37.0	36.8
Industry products	17.3	19.1	19.3
Ceramic tile	4.3	4.3	13.5
Corporate	8.1	9.4	5.6
Total depreciation and amortization	\$ 132.7	\$ 123.7	\$ 123.1
Capital additions: (Note 3)			
Floor coverings	\$ 76.6	\$ 117.7	\$ 77.3
Building products	54.4	67.7	49.2
Industry products	16.5	22.5	45.0
Ceramic tile	--	--	9.6
Corporate	8.7	12.8	6.3
Total capital additions	\$ 156.2	\$ 220.7	\$ 187.4
Identifiable assets:			
Floor coverings	\$ 713.8	\$ 687.9	\$ 583.2
Building products	554.9	541.1	513.5
Industry products	248.6	272.8	301.8
Ceramic tile	135.7	168.7	135.8
Corporate	722.5	465.1	615.5
Total assets	\$2,375.5	\$2,135.6	\$2,149.8

Note 1:

Restructuring charges in operating income (millions)	1997	1996	1995
Floor coverings	\$ --	\$ 14.5	\$ 25.0
Building products	--	8.3	6.3
Industry products	--	4.0	31.4
Unallocated corporate expense	--	19.7	9.1

Total restructuring charges			
in operating income	\$ --	\$ 46.5	\$ 71.8

Note 2: 1997 operating income includes a \$29.7 million loss as a result of charges incurred by Dal-Tile International Inc. for uncollectible receivables, overstocked inventories and other asset revaluations. 1995 operating income includes a \$177.2 million loss due to the ceramic tile business combination. See "Equity Earnings From Affiliates" on page 4.

Note 3: 1997 and 1995 capital additions for industry segments of property, plant and equipment from acquisitions were \$14.5 million and \$15.6 million, respectively.

DISCONTINUED OPERATIONS

In 1995 the company sold the stock of its furniture subsidiary, Thomasville Furniture Industries, Inc., to INTERCO Incorporated for \$331.2 million in cash. INTERCO also assumed \$8.0 million of interest-bearing debt. The company recorded a gain of \$83.9 million after tax on the sale. Certain liabilities related to terminated benefit plans of approximately \$11.3 million were retained by the company. Thomasville and its subsidiaries recorded sales of approximately \$550.2 million in 1995.

EQUITY (EARNINGS) LOSS FROM AFFILIATES

Equity earnings from affiliates for 1997 were primarily comprised of the company's share of the net loss from the Dal-Tile International Inc. business combination and the amortization of the excess of the company's investment in Dal-Tile over the underlying equity in net assets, and income from the 50% interest in the WAVE joint venture with Worthington Industries. The 1997 loss included \$8.4 million for the company's share of operating losses incurred by Dal-Tile, a \$29.7 million loss for the company's share of the charge incurred by Dal-Tile, primarily for uncollectible receivables and overstocked inventories, and \$4.3 million for the amortization of Armstrong's initial investment in Dal-Tile over the underlying equity in net assets of the business combination. Equity earnings from affiliates for 1996 were primarily comprised of the company's after-tax share of the net income of the Dal-Tile International Inc. business combination and the amortization of the excess of the company's investment in Dal-Tile over the underlying equity in net assets, and the 50% interest in the WAVE joint venture with Worthington Industries. Results in 1995 reflect only the 50% interest in the WAVE joint venture.

In 1995, the company entered into a business combination with Dal-Tile International Inc. The transaction was accounted for at fair value and involved the exchange of \$27.6 million in cash and the stock of the ceramic tile operations, consisting primarily of American Olean Tile Company, a wholly-owned subsidiary, for ownership of 37% of the shares of Dal-Tile. The company's investment in Dal-Tile exceeded the underlying equity in net assets by \$123.9 million which will be amortized over a period of 30 years. The after-tax loss on the transaction was \$116.8 million.

In August 1996, Dal-Tile issued new shares in a public offering decreasing the company's ownership share from 37% to 33%. During 1997, the company purchased additional shares of Dal-Tile stock, increasing the company's ownership to 34%.

Armstrong's ownership of Dal-Tile is accounted for under the equity method. The summarized historical financial information for ceramic tile operations is presented below.

(millions)	1995
Net sales	\$240.1
Operating income/(1)/	8.8
Assets/(2)/	269.8
Liabilities/(2)/	17.3

Note 1: Excludes 1995 loss of \$177.2 million due to ceramic tile business combination.

Note 2: 1995 balances were as of December 29, 1995, immediately prior to the ceramic tile business combination.

Narrative Description of Business

The Company manufactures and sells interior furnishings, including floor coverings and building products, and makes and markets a variety of specialty products for the building, automotive, textile, and other industries. The Company's activities extend worldwide.

Floor Coverings

The Company is a prominent worldwide manufacturer of floor coverings for the interiors of homes and commercial and institutional buildings, with a broad range of resilient flooring together with adhesives, installation and maintenance materials and accessories. Resilient flooring, in both sheet and tile form, together with laminate flooring, is made in a wide variety of types, designs, and colors. Included are types of flooring that offer such features as ease of installation, reduced maintenance (no-wax), and cushioning for greater underfoot comfort. Floor covering products are sold to the commercial and residential market segments through wholesalers, retailers (including large home centers), and contractors, and to the hotel/motel and manufactured homes industries.

Building Products

A major producer of ceiling materials in the United States and abroad, the Company markets both residential and commercial ceiling systems. Ceiling materials for the home are offered in a variety of types and designs; most provide noise reduction and incorporate Company-designed features intended to permit ease of installation. These residential ceiling products are sold through wholesalers and retailers (including large home centers). Commercial ceiling systems, designed for use in shopping centers, offices, schools, hospitals, and other commercial and institutional structures, are available in numerous colors, performance characteristics and designs and offer characteristics such as acoustical control, rated fire protection, and aesthetic appeal. Commercial ceiling materials and accessories, along with acoustical wall panels, are sold by the Company to ceiling systems contractors and to resale distributors. Suspension ceiling systems products are manufactured and sold through a joint venture with Worthington Industries.

Industry Products

The Company, including a number of its subsidiaries, manufactures and markets a variety of specialty products for the building, automotive, textile and other industries. These products include flexible pipe insulation sold for use in construction and in original equipment manufacture; gasket materials for new equipment and replacement use in the automotive, farm equipment, appliance, and other industries; textile mill supplies including cots and aprons sold to equipment manufacturers and textile mills. Industry products are sold, depending on type and ultimate use, to original equipment manufacturers, contractors, wholesalers, fabricators and end users.

Ceramic Tile

Ceramic tile for floors, walls and countertops, together with adhesives, installation and maintenance materials and accessories are sold through home centers, independent ceramic and floor covering wholesalers and sales service centers operated by Dal-Tile.

The principal raw materials used in the manufacture of the Company's products are synthetic resins, plasticizers, latex, mineral fibers and fillers, clays, starches, perlite, films, pigments and inks. In addition, the Company uses a wide variety of other raw materials. Most raw materials are purchased from sources outside of the Company. The Company also purchases significant amounts of packaging materials for the containment and shipment of its various

products. During 1997, adequate supplies of raw materials were available to all of the Company's industry segments.

Customers' orders for the Company's products are typically for immediate shipment. Thus, in each industry segment, the Company has implemented inventory systems, including its "just in time" inventory system, pursuant to which orders are promptly filled out of inventory on hand or the product is manufactured to meet the delivery date specified in the order. As a result, there historically has been no material backlog in any industry segment.

The competitive position of the Company has been enhanced by patents on products and processes developed or perfected within the Company or obtained through acquisition. Although the Company considers that, in the aggregate, its patents constitute a valuable asset, it does not regard any industry segment as being materially dependent upon any single patent or any group of related patents.

There is significant competition in all of the industry segments in which the Company does business. Competition in each industry segment includes numerous active companies (domestic and foreign), with emphasis on price, product performance and service. In addition, with the exception of industrial and other products and services, product styling is a significant method of competition in the Company's industry segments. Increasing domestic competition from foreign producers is apparent in certain industry segments and actions continue to be taken to meet this competition.

The Company invested \$141.7 million in 1997, \$220.7 million in 1996, and \$171.8 million in 1995 for additions to the property, plant and equipment of its continuing businesses.

Research and development activities are important and necessary in assisting the Company to carry on and improve its business. Principal research and development functions include the development of new products and processes and the improvement of existing products and processes.

The Company spent \$47.8 million in 1997, \$55.2 million in 1996, and \$57.9 million in 1995 on research and development activities worldwide for the continuing businesses.

ENVIRONMENTAL MATTERS

In 1997, the company incurred capital expenditures of approximately \$1.2 million for environmental compliance and control facilities and anticipates comparable annual expenditures for those purposes for the years 1998 and 1999. The company does not anticipate that it will incur significant capital expenditures in order to meet the requirements of the Clean Air Act of 1990 and the final implementing regulations promulgated by various state agencies.

As with many industrial companies, Armstrong is currently involved in proceedings under the Comprehensive Environmental Response, Compensation and Liability Act ("Superfund"), and similar state laws at approximately 17 sites. In most cases, Armstrong is one of many potentially responsible parties ("PRPs") who have voluntarily agreed to jointly fund the required investigation and remediation of each site. With regard to some sites, however, Armstrong disputes the liability, the proposed remedy or the proposed cost allocation. Armstrong may also have rights of contribution or reimbursement from other parties or coverage under applicable insurance policies. The company is also remediating environmental contamination resulting from past industrial activity at certain of its current plant sites.

Estimates of future liability are based on an evaluation of currently available facts regarding each individual site and consider factors including existing technology, presently enacted laws and regulations and prior company experience in remediation of contaminated sites. Although current law imposes joint and several liability on all parties at any Superfund site, Armstrong's contribution to the remediation of these sites is expected to be limited by the number of other companies also identified as potentially liable for site costs. As a result, the company's estimated liability reflects only the company's expected share. In determining the probability of contribution, the company considers the solvency of the parties, whether responsibility, is being disputed, the terms of any existing agreements and experience regarding similar matters. The estimated liabilities do not take into account any claims for recoveries from insurance or third parties.

Reserves at December 31, 1997, were for potential environmental liabilities that the company considers probable and for which a reasonable estimate of the potential liability could be made. Where existing data is sufficient to estimate the amount of the liability, that estimate has been used; where only a range of probable liability is available and no amount within that range is more likely than any other, the lower end of the range has been used. As a result, the company has accrued, before agreed-to insurance coverage, \$9.3 million to reflect its estimated undiscounted liability for environmental remediation. As assessments and remediation activities progress at each individual site, these liabilities are reviewed to reflect additional information as it becomes available.

Actual costs to be incurred at identified sites in the future may vary from the estimates, given the inherent uncertainties in evaluating environmental liabilities. Subject to the imprecision in estimating environmental remediation costs, the company believes that any sum it may have to pay in connection with environmental matters in excess of the amounts noted above would not have a material adverse effect on its financial condition, liquidity or results of operations, although the recording of future costs may be material to earnings in such future period.

As of December 31, 1997, the Company had approximately 10,600 active employees, of whom approximately 3,800 are located outside the United States. About 62% of the Company's approximately 4,300 hourly or salaried production and maintenance employees in the United States are represented by labor unions.

GEOGRAPHIC AREAS

at December 31 (millions)	1997	1996	1995

Net trade sales:			
United States	\$1,453.1	\$1,419.2	\$1,586.4
Europe	545.6	548.4	558.7
Other foreign	200.0	188.8	179.9

Interarea transfers:			
United States	111.7	105.0	101.1
Europe	14.9	13.2	13.8
Other foreign	29.2	30.4	32.1
Eliminations	(155.8)	(148.6)	(147.0)

Total net sales	\$2,198.7	\$2,156.4	\$2,325.0
=====			
Operating income:			
United States (see note 2 on page 4)	\$ 236.1	\$ 202.7	\$ 7.7
Europe	77.2	79.3	62.6
Other foreign	8.6	10.0	7.8
Unallocated corp. income (expense)	0.1	(36.1)	(34.0)

Total operating income	\$ 322.0	\$ 255.9	\$ 44.1
=====			
Identifiable assets:			
United States	\$1,168.9	\$1,180.1	\$1,044.5
Europe	370.4	383.7	406.7
Other foreign	113.8	107.3	83.4
Corporate	722.5	465.1	615.5
Eliminations	(0.1)	(0.6)	(0.3)

Total assets	\$2,375.5	\$2,135.6	\$2,149.8
=====			

United States net trade sales include export sales to non-affiliated customers of \$40.9 million in 1997, \$34.0 million in 1996 and \$32.1 million in 1995. Also included in United States net trade sales were ceramic tile operations sales of \$240.1 million in 1995.

"Europe" includes operations located primarily in England, France, Germany, Italy, the Netherlands, Poland, Spain, Sweden and Switzerland. Operations in Australia, Canada, The People's Republic of China, Hong Kong, Indonesia, Japan, Korea, Singapore and Thailand are in "Other foreign."

Transfers between geographic areas and commissions paid to affiliates marketing exported products are accounted for by methods that approximate arm's-length transactions, after considering the costs incurred by the selling company and the return on assets employed of both the selling unit and the purchasing unit. Operating income of a geographic area includes income accruing from sales to affiliates.

The Company's foreign operations are subject to foreign government legislation involving restrictions on investments (including transfers thereof), tariff restrictions, personnel administration, and other actions by foreign governments. In addition, consolidated earnings are subject to both U.S. and foreign tax laws with respect to earnings of foreign subsidiaries, and to the effects of currency fluctuations.

Item 2. Properties

The Company produces and markets its products and services throughout the world, operating 44 manufacturing plants in 13 countries; 21 of these plants are located throughout the United States. Additionally, affiliates operate 19 plants in 6 countries.

Floor covering products and adhesives are produced at 16 plants with principal manufacturing facilities located in Lancaster, Pennsylvania, Kankakee, Illinois, and Stillwater, Oklahoma. Building products are produced at 15 plants with principal facilities in Macon, Georgia, the Florida-Alabama Gulf Coast area and Marietta, Pennsylvania. Insulating materials, textile mill supplies, fiber gasket materials and specialty papers and other products for industry are manufactured at 16 plants with principal manufacturing facilities at Munster, Germany, and Fulton, New York.

Sales offices are leased worldwide, and leased facilities are utilized to supplement the Company's owned warehousing facilities.

Productive capacity and extent of utilization of the Company's facilities are difficult to quantify with certainty because in any one facility, maximum capacity and utilization vary periodically depending upon the product that is being manufactured and individual facilities manufacture more than one type of product. In this context, the Company estimates that the production facilities in each of its industry segments were effectively utilized during 1997 at 80% to 90% of overall productive capacity in meeting market conditions. Remaining productive capacity is sufficient to meet expected customer demands.

The Company believes its various facilities are adequate and suitable. Additional incremental investments in plant facilities are being made as appropriate to balance capacity with anticipated demand, improve quality and service, and reduce costs.

Item 3. Legal Proceedings

ASBESTOS-RELATED LITIGATION

PERSONAL INJURY LITIGATION

The company is one of many defendants in approximately 83,000 pending claims as of December 31, 1997, alleging personal injury from exposure to asbestos. The increase in the number of claims during the last two quarters of 1997 is primarily due to the inclusion of cases that had been subject to an injunction related to the Georgine Settlement Class Action ("Georgine"), described below, and those that had been filed in the tort system against other defendants (and not against the Center for Claims Resolution ("Center") members) while Georgine was pending.

Nearly all claims seek general and punitive damages arising from alleged exposures, at various times, from World War II onward, to asbestos-containing products. Claims against the company generally involve allegations of negligence, strict liability, breach of warranty and conspiracy with respect to its involvement with asbestos-containing insulation products. The company discontinued the sale of all such products in 1969. The claims also allege that injury may be determined many years (up to 40 years) after first exposure to asbestos. Nearly all suits name many defendants, and over 100 different companies are reportedly involved. The company believes that many current plaintiffs are unimpaired. A large number of claims have been settled, dismissed, put on inactive lists or otherwise resolved, and the company generally is involved in all stages of claims resolution and litigation, including individual trials, consolidated trials and appeals. Neither the rate of future filings and resolutions nor the total number of future claims can be predicted at this time with a high degree of certainty.

Attention has been given by various parties to securing a comprehensive resolution of the litigation. In 1991, the Judicial Panel for Multidistrict Litigation ordered the transfer of federal cases to the Eastern District of Pennsylvania in Philadelphia for pretrial purposes. The company supported this transfer. Some cases are periodically released for trial, although the issue of punitive damages is retained by the transferee court. That court has been instrumental in having the parties resolve large numbers of cases in various jurisdictions and has been receptive to different approaches to the resolution of claims. Claims in state courts have not been directly affected by the transfer, although most recent cases have been filed in state courts.

Georgine Settlement Class Action

Georgine v. Amchem was a settlement class action filed in the Eastern District of Pennsylvania, on January 15, 1993, that included essentially all future personal injury claims against members of the Center, including the company. It was designed to establish a nonlitigation system for the resolution of such claims, and offered a method for prompt compensation to claimants who were occupationally exposed to asbestos if they met certain exposure and medical criteria. Compensation amounts were derived from historical settlement data and no punitive damages were to be paid. The settlement was designed to, among other things, minimize transactional costs, including attorneys' fees, expedite compensation to claimants with qualifying claims, and relieve the courts of the burden of handling future claims. Based on maximum mathematical projections covering a ten-year period starting in 1994, the company estimated in Georgine a reasonably possible additional liability of \$245 million.

The District Court, after exhaustive discovery and testimony, approved the settlement class action and issued a preliminary injunction that barred class members from pursuing claims against Center members in the tort system. The U.S. Court of Appeals for the Third Circuit reversed that decision, and the reversal was sustained by the U.S. Supreme Court on June 25, 1997, holding that the settlement class did not meet the requirements for class certification under Federal Rule of Civil Procedure 23. The preliminary injunction was vacated on July 21, 1997, resulting in the immediate reinstatement of enjoined cases and a loss of the bar against the filing of claims in the tort system. The company believes that an alternative claims resolution mechanism to Georgine is likely to emerge.

Asbestos-related liability

During the last half of 1997, the company assessed the impact of the recent Supreme Court ruling on its projected asbestos resolution and defense costs. In doing so, the company reviewed, among other things, its historical settlement amounts, the incidence of past claims, the mix of the injuries and occupations of the plaintiffs, the number of cases pending against it, the Georgine projection and its experience. Subject to the uncertainties, limitations and other factors referred to above and based upon its experience, the company has recorded \$251.7 million on the balance sheet as an estimated minimum liability to defend and resolve probable and estimable asbestos-related personal injury claims currently pending and to be filed through 2003. This is management's best estimate of the minimum liability, although potential future costs for claims could range up to an additional \$387 million or an estimated maximum liability of approximately \$639 million. Because of the uncertainties related to asbestos litigation, it is not possible to estimate the number of personal injury claims that may be filed after 2003 or their defense and resolution costs. Therefore, the company's estimated liability does not include costs for personal injury claims that may be filed after 2003, although it is likely there will be such additional claims. Management believes that the potential additional costs for claims to be filed through 2003 and those filed thereafter, net of any potential insurance recoveries, will not have a material after-tax effect on the financial condition of the company or its liquidity, although the net after-tax effect of any future liabilities recorded in excess of insurance assets could be material to earnings in a future period.

PROPERTY DAMAGE LITIGATION

The company is also one of many defendants in 10 pending claims as of December 31, 1997, brought by public and private building owners. These claims include allegations of damage to buildings caused by asbestos-containing products and generally seek compensatory and punitive damages and equitable relief, including reimbursement of expenditures, for removal and replacement of such products. The claims appear to be aimed at friable (easily crumbled) asbestos-containing products, although allegations encompass all asbestos-containing products, including previously installed asbestos-containing resilient flooring. Among the lawsuits that have been resolved are four class actions, which involve public and private schools, Michigan state public and private schools, colleges and universities, and private property owners who leased facilities to the federal government. The company vigorously denies the validity of the allegations against it in these claims. These suits and claims are not handled by the Center. Insurance coverage has been resolved and is expected to cover almost all costs of these claims.

CODEFENDANT BANKRUPTCIES

Certain codefendant companies have filed for reorganization under Chapter 11 of the Federal Bankruptcy Code. As a consequence, litigation against them (with some exceptions) has been stayed or restricted. Due to the uncertainties involved, the long-term effect of these proceedings on the litigation cannot be predicted.

INSURANCE COVERAGE

The company's primary and excess insurance policies provide product hazard and nonproducts (general liability) coverages for personal injury claims, and product hazard coverage for property damage claims. Certain policies also provide coverage to ACandS, Inc., a former subsidiary of the company. The company and ACandS, Inc., share certain limits that both have accessed and have entered into an agreement that reserved for ACandS, Inc., a certain amount of excess insurance.

California Insurance Coverage Lawsuit

Trial court decisions in the insurance lawsuit filed by the company in California held that the trigger of coverage for personal injury claims was continuous from exposure through death or filing of a claim, that a triggered insurance policy should respond with full indemnification up to policy limits, and that any defense obligation ceases upon exhaustion of policy limits. Although not as comprehensive, another decision established favorable defense and indemnity coverage for property damage claims, providing coverage during the period of installation and any subsequent period in which a release of fibers occurred. The California appellate courts substantially upheld the trial court, and that insurance coverage litigation is now concluded. The company has resolved most personal injury products hazard coverage matters with its solvent carriers through the Wellington Agreement, referred to below, or other settlements. In 1989, a settlement with a carrier having both primary and excess coverages provided for certain minimum and maximum percentages of costs for personal injury claims to be allocated to nonproducts (general liability) coverage, the percentage to be determined by negotiation or in alternative dispute resolution ("ADR").

The insurance carriers that provided personal injury products hazard, nonproducts or property damage coverages are as follows: Reliance Insurance Company; Aetna (now Travelers) Casualty and Surety Company; Liberty Mutual Insurance Company; Travelers Insurance Company; Fireman's Fund Insurance Company; Insurance Company of North America; Lloyds of London; various London market companies; Fidelity and Casualty Insurance Company; First State Insurance Company; U.S. Fire Insurance Company; Home Insurance Company; Great American Insurance Company; American Home Assurance Company and National Union Fire Insurance Company (known as the AIG Companies); Central National Insurance Company; Interstate Insurance Company; Puritan Insurance Company; and Commercial Union Insurance Company. Midland Insurance Company, an excess carrier that provided \$25 million of personal injury coverage, certain London companies, and certain excess carriers providing only property damage coverage are insolvent. The company is pursuing claims against insolvents in a number of forums.

Wellington Agreement

In 1985, the company and 52 other companies (asbestos defendants and insurers) signed the Wellington Agreement. This Agreement settled nearly all disputes concerning personal injury insurance coverage with most of the company's carriers, provided broad coverage for both defense and indemnity and addressed both products hazard and non-products (general liability) coverages.

Asbestos Claims Facility ("Facility") and Center for Claims Resolution

The Wellington Agreement established the Facility to evaluate, settle, pay and defend all personal injury claims against member companies. Resolution and defense costs were allocated by formula. The Facility subsequently dissolved, and the Center was created in October 1988 by 21 former Facility members, including the company. Insurance carriers, while not members, are represented ex officio on the Center's governing board and have agreed annually to provide a portion of the Center's operational costs. The Center adopted many of the conceptual features of the Facility and has addressed the claims in a manner consistent with the prompt, fair resolution of meritorious claims. Resolution and defense costs are allocated by formula; adjustments over time have resulted in some increased share for the company.

Insurance Recovery Proceedings

A substantial portion of the company's primary and excess insurance asset is nonproducts (general liability) insurance for personal injury claims, including among others, those that involve exposure during installation of asbestos materials. The Wellington Agreement and the 1989 settlement agreement referred to above have provisions for such coverage. An ADR process under the Wellington Agreement is underway against certain carriers to determine the percentage of resolved and unresolved claims that are nonproducts claims, to establish the entitlement to such coverage and to determine whether and how much reinstatement of prematurely exhausted products hazard insurance is warranted. The nonproducts coverage potentially available is substantial and, for some policies, includes defense costs in addition to limits. The carriers have raised various defenses, including waiver, laches, statutes of limitations and contractual defenses. One primary carrier alleges that it is no longer bound by the Wellington Agreement, and another alleges that the company agreed to limit its claims for nonproducts coverage against that carrier when the Wellington Agreement was signed. The ADR process is in the trial phase of binding arbitration. Other proceedings against non-Wellington carriers may become necessary.

An insurance asset in the amount of \$291.6 million is recorded on the balance sheet and reflects the company's belief in the availability of insurance in this amount, based upon the company's success in insurance recoveries, settlement agreements that provide such coverage, the nonproducts recoveries by other companies and the opinion of outside counsel. Such insurance is probable of recovery through negotiation or litigation. A substantial portion of the insurance asset is in ADR, which the company believes may be resolved in 1998 or later. A shortfall has developed between available insurance and amounts necessary for resolution and defense costs. This shortfall was \$39.9 million at the end of 1997 and included a \$1.5 million insurance recovery from an insolvent insurance carrier. The recovery of insurance assets to cover the shortfall will depend upon the resolution of the ADR and other disputes with the insurance carriers. The company does not believe that after-tax effect of the shortfall will be material either to the financial condition of the company or to its liquidity.

CONCLUSIONS

The company does not know how many claims will be filed against it in the future, or the details thereof or of pending suits not fully reviewed, or the defense and resolution costs that may ultimately result therefrom, or whether an alternative to the Georgine settlement vehicle may emerge, or the scope of its insurance coverage ultimately deemed available.

The company has assessed the impact of the recent Supreme Court ruling on its projected asbestos resolution and defense costs. Subject to the uncertainties, limitations and other factors referred to above and based upon its experience, the company has recorded on the balance sheet \$251.7 million as a minimum estimated liability to defend and resolve probable and estimable asbestos-related personal injury claims currently pending and to be filed through 2003.

This is management's best estimate of the minimum liability, although potential future costs for these claims could range up to an additional \$387 million or an estimated maximum liability of approximately \$639 million. Because of the uncertainties related to asbestos litigation, it is not possible to estimate the number of personal injury claims that may be filed after 2003 or their cost. Therefore, the company's estimated liability does not include costs for personal injury claims that may be filed after 2003, although it is likely there will be such additional claims. Management believes that the potential additional costs for claims to be filed through 2003 and those filed thereafter, net of any potential insurance recoveries, will not have a material after-tax effect on the financial condition of the company or its liquidity, although the net after-tax effect of any future liabilities recorded in excess of insurance assets could be material to earnings in a future period.

An insurance asset in the amount of \$291.6 million is recorded on the balance sheet and reflects the company's belief in the availability of insurance in this amount, based upon the company's success in insurance recoveries, settlement agreements that provide such coverage, the nonproducts recoveries by other companies, and the opinion of outside counsel. Such insurance is probable of recovery through negotiation or litigation. A substantial portion of the insurance asset is in ADR, which the company believes may be resolved in 1998 or later. A shortfall has developed between available insurance and amounts necessary for resolution and defense costs. This shortfall was \$39.9 million at the end of 1997 and included a \$1.5 million insurance recovery from an insolvent insurance carrier. The recovery of insurance assets to cover the shortfall will depend upon the resolution of the ADR and other disputes with the insurance carriers. The company does not believe that after-tax effect of the shortfall will be material either to the financial condition of the company or to its liquidity.

The company believes that a claims resolution mechanism alternative to the Georgine settlement will eventually emerge, and that the resolution and defense costs are likely to be higher than the earlier maximum mathematical projection in Georgine.

Subject to the uncertainties, limitations and other factors referred to elsewhere in this note and based upon its experience, the company believes it is probable that substantially all of the defense and resolution costs of property damage claims will be covered by insurance.

Even though uncertainties remain as to the potential number of unasserted claims and the liability resulting therefrom, and after consideration of the factors involved, including the ultimate scope of its insurance coverage, the Wellington Agreement and other settlements with insurance carriers, the results of the California insurance coverage litigation, the establishment of the Center, the likelihood that an alternative to the Georgine settlement will eventually emerge, and its experience, the company believes the asbestos-related claims against the company would not be material either to the financial condition of the company or to its liquidity, although the net after-tax effect of any future liabilities recorded in excess of insurance assets could be material to earnings in such future period.

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

Not applicable.

Executive Officers of the Registrant

The information appearing in Item 10 hereof under the caption "Executive Officers of the Registrant" is incorporated by reference herein.

PART II

Item 5. Market for the Registrant's Common Equity and Related Stockholder

Matters

The Company's Common Stock is traded on the New York Stock Exchange, Inc., the Philadelphia Stock Exchange, Inc., and the Pacific Stock Exchange, Inc. As of February 10, 1998, there were approximately 7,100 holders of record of the Company's Common Stock.

During 1997, the Company issued a total of 1,800 shares of Common Stock to nonemployee directors of the Company pursuant to the Company's Restricted Stock Plan for Nonemployee Directors. Given the small number of persons to whom these shares were issued, applicable restrictions on transfer and the information regarding the Company possessed by the directors, these shares were issued without registration in reliance on Section 4(2) of the Securities Act of 1933, as amended.

Quarterly Financial Information

		First	Second	Third	Fourth	Total year
1997	Dividends per share of common stock	0.40	0.44	0.44	0.44	1.72
	Price range of common stock--high	72 1/4	75 1/4	74 9/16	75 3/8	75 3/8
	Price range of common stock--low	64 3/4	61 1/2	64 3/8	64 1/8	61 1/2
1996	Dividends per share of common stock	0.36	0.40	0.40	0.40	1.56
	Price range of common stock--high	64 1/2	61 5/8	65 1/2	75 1/4	75 1/4
	Price range of common stock--low	57 7/8	53 1/2	51 7/8	61 3/4	51 7/8

Item 6. Selected Financial Data

ELEVEN-YEAR SUMMARY

(Dollars in millions except for per-share data)	For year	1997	1996	1995	1994
Net sales		2,198.7	2,156.4	2,325.0	2,226.0
Cost of goods sold		1,461.7	1,459.9	1,581.1	1,483.9
Total selling, general and administrative expenses		385.3	413.2	457.0	449.2
Equity (earnings) loss from affiliates		29.7	(19.1)	(6.2)	(1.7)
Restructuring charges		--	46.5	71.8	--
Loss from ceramic tile business formation/ (gain) from sales of woodlands		--	--	177.2	--
Operating income (loss)		322.0	255.9	44.1	294.6
Interest expense		28.0	22.6	34.0	28.3
Other expense (income), net		(2.2)	(6.9)	1.9	0.5
Earnings (loss) from continuing businesses before income taxes		296.2	240.2	8.2	265.8
Income taxes		111.2	75.4	(5.4)	78.6
Earnings (loss) from continuing businesses		185.0	164.8	13.6	187.2
As a percentage of sales		8.4%	7.6%	0.6%	8.4%
As a percentage of average monthly assets (a)		9.0%	8.5%	0.7%	10.7%
Earnings (loss) from continuing businesses applicable to common stock (b)		185.0	158.0	(0.7)	173.1
Per common share--basic (c)		4.55	4.04	(0.02)	4.62
Per common share--diluted (c)		4.50	3.82	(0.02)	4.09
Net earnings (loss)		185.0	155.9	123.3	210.4
As a percentage of sales		8.4%	7.2%	5.3%	9.5%
Net earnings (loss) applicable to common stock (b)		185.0	149.1	109.0	196.3
As a percentage of average shareholders' equity		22.3%	19.6%	15.0%	31.3%
Per common share--basic (c)		4.55	3.81	2.94	5.24
Per common share--diluted (c)		4.50	3.61	2.68	4.62
Dividends declared per share of common stock		1.72	1.56	1.40	1.26
Capital expenditures		160.5	228.0	182.7	138.4
Aggregate cost of acquisitions		4.2	--	20.7	--
Total depreciation and amortization		132.7	123.7	123.1	120.7
Average number of employees--continuing businesses		10,643	10,572	13,433	13,784
Average number of common shares outstanding (millions)		40.6	39.1	37.1	37.5
Year-end position					
Working capital--continuing businesses		128.5	243.5	346.8	384.4
Net property, plant and equipment--continuing businesses		972.2	964.0	878.2	966.4
Total assets		2,375.5	2,135.6	2,149.8	2,159.0
Net long-term debt		223.1	219.4	188.3	237.2
Total debt as a percentage of total capital (d)		39.2%	37.2%	38.5%	41.4%
Shareholders' equity		810.6	790.0	775.0	735.1
Book value per share of common stock		20.20	19.19	20.10	18.97
Number of shareholders (e) (f)		7,137	7,424	7,084	7,473
Common shares outstanding (millions)		40.1	41.2	36.9	37.2
Market value per common share		74 3/4	69 1/2	62	38 1/2

		1993	1992	1991	1990
Net sales		2,075.7	2,111.4	2,021.4	2,082.4
Cost of goods sold		1,453.7	1,536.1	1,473.7	1,469.8
Total selling, general and administrative expenses		435.6	446.6	415.1	404.0
Equity (earnings) loss from affiliates		(1.4)	(0.2)	--	--
Restructuring charges		89.3	160.8	12.5	6.8
Loss from ceramic tile business formation/ (gain) from sales of woodlands		--	--	--	(60.4)
Operating income (loss)		98.5	(31.9)	120.1	262.2
Interest expense		38.0	41.6	45.8	37.5
Other expense (income), net		(6.1)	(7.2)	(8.5)	19.7
Earnings (loss) from continuing businesses before income taxes		66.6	(66.3)	82.8	205.0
Income taxes		17.6	(2.9)	32.7	69.5
Earnings (loss) from continuing businesses		49.0	(63.4)	50.1	135.5
As a percentage of sales		2.4%	-3.0%	2.5%	6.5%
As a percentage of average monthly assets (a)		2.8%	-3.3%	2.7%	7.5%
Earnings (loss) from continuing businesses applicable to common stock (b)		35.1	(77.2)	30.7	116.0
Per common share--basic (c)		0.95	(2.08)	0.83	2.98
Per common share--diluted (c)		0.93	(2.08)	0.83	2.73
Net earnings (loss)		63.5	(227.7)	48.2	141.0
As a percentage of sales		3.1%	-10.8%	2.4%	6.8%
Net earnings (loss) applicable to common stock (b)		49.6	(241.5)	28.8	121.5
As a percentage of average shareholders' equity		9.0%	-33.9%	3.3%	13.0%
Per common share--basic (c)		1.34	(6.51)	0.78	3.12
Per common share--diluted (c)		1.27	(6.51)	0.78	2.86
Dividends declared per share of common stock		1.20	1.20	1.19	1.135
Capital expenditures		110.3	109.8	129.7	186.5
Aggregate cost of acquisitions		--	4.2	--	16.1
Total depreciation and amortization		117.0	123.4	122.1	116.5
Average number of employees--continuing businesses		14,796	16,045	16,438	16,926
Average number of common shares outstanding (millions)		37.2	37.1	37.1	38.9
Year-end position					
Working capital--continuing businesses		279.3	239.8	353.8	305.2
Net property, plant and equipment--continuing businesses		937.6	967.2	1,042.8	1,032.7
Total assets		1,869.2	1,944.3	2,125.7	2,124.4
Net long-term debt		256.8	266.6	301.4	233.2

Total debt as a percentage of total capital (d)	52.2%	57.2%	46.9%	45.7%
Shareholders' equity	569.5	569.2	885.5	899.2
Book value per share of common stock	14.71	14.87	23.55	24.07
Number of shareholders (e) (f)	7,963	8,611	8,896	9,110
Common shares outstanding (millions)	37.2	37.1	37.1	37.1
Market value per common share	53 1/4	31 7/8	29 1/4	25

	1989	1988	1987
Net sales	2,050.4	1,843.4	1,608.7
Cost of goods sold	1,423.2	1,287.6	1,112.0
Total selling, general and administrative expenses	380.7	331.3	288.8
Equity (earnings) loss from affiliates	--	--	--
Restructuring charges	5.9	--	--
Loss from ceramic tile business formation/ (gain) from sales of woodlands	(9.5)	(1.9)	--
Operating income (loss)	250.1	226.4	207.9
Interest expense	40.5	25.8	11.5
Other expense (income), net	(5.7)	(13.1)	(4.3)
Earnings (loss) from continuing businesses before income taxes	215.3	213.7	200.7
Income taxes	74.6	79.4	82.2
Earnings (loss) from continuing businesses	140.7	134.3	118.5
As a percentage of sales	6.9%	7.3%	7.4%
As a percentage of average monthly assets (a)	8.6%	10.4%	11.3%
Earnings (loss) from continuing businesses applicable to common stock (b)	131.0	133.9	118.0
Per common share--basic (c)	2.88	2.90	2.50
Per common share--diluted (c)	2.75	2.88	2.49
Net earnings (loss)	187.6	162.7	150.4
As a percentage of sales	9.1%	8.8%	9.3%
Net earnings (loss) applicable to common stock (b)	177.9	162.3	150.0
As a percentage of average shareholders' equity	17.9%	17.0%	17.6%
Per common share--basic (c)	3.92	3.51	3.18
Per common share--diluted (c)	3.72	3.50	3.16
Dividends declared per share of common stock	1.045	0.975	0.885
Capital expenditures	216.9	167.8	157.6
Aggregate cost of acquisitions	--	355.8	71.5
Total depreciation and amortization	121.6	99.4	83.6
Average number of employees--continuing businesses	17,167	15,016	14,036
Average number of common shares outstanding (millions)	45.4	46.2	47.2

Year-end position			
Working capital--continuing businesses	449.4	260.6	345.3
Net property, plant and equipment--continuing businesses	944.0	930.4	674.1
Total assets	2,008.9	2,073.1	1,574.9
Net long-term debt	181.3	185.9	67.7
Total debt as a percentage of total capital (d)	36.1%	35.9%	22.8%
Shareholders' equity	976.5	1,021.8	913.8
Book value per share of common stock	23.04	21.86	19.53
Number of shareholders (e) (f)	9,322	10,355	9,418
Common shares outstanding (millions)	42.3	46.3	46.2
Market value per common share	37 1/4	35	32 1/4

Notes:

- (a) Assets exclude insurance recoveries for asbestos-related liabilities.
- (b) After deducting preferred dividend requirements and adding the tax benefits for unallocated preferred shares.
- (c) See definition of basic and diluted earnings per share on page 35. Earnings per share data is restated for all periods for adoption of SFAS No. 128.
- (d) Total debt includes short-term debt, current installments of long-term debt, long-term debt and ESOP loan guarantee. Total capital includes total debt and total shareholders' equity.
- (e) Includes one trustee who is the shareholder of record on behalf of approximately 6,000 to 6,500 employees for years 1988 through 1997.
- (f) Includes, for 1987, a trustee who was the shareholder of record on behalf of approximately 11,000 employees who obtained beneficial ownership through the Armstrong Stock Ownership Plan, which was terminated at the end of 1987.

Beginning in 1996, ceramic tile results were reported under the equity method, whereas prior to 1996, ceramic tile operations were reported on a consolidated or line item basis.

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

1997 COMPARED WITH 1996

FINANCIAL CONDITION

As shown on the Consolidated Statements of Cash Flows (see page 33), the company had cash and cash equivalents of \$57.9 million at December 31, 1997. Cash provided by operating activities, supplemented by increases in short-term debt; proceeds from the sale of land, facilities and other assets, and cash proceeds from exercised stock options, covered normal working capital requirements; purchases of property, plant and equipment; payment of cash dividends; repurchase of shares; acquisitions and investments in joint ventures and computer software.

Cash provided by operating activities for the year ended December 31, 1997, was \$246.6 million compared with \$220.9 million in 1996. The increase is primarily due to the higher level of earnings before noncash charges and lower restructuring payments year-to-year, partially offset by the payment of cash due to a shortfall between currently available insurance and amounts necessary to pay asbestos-related claims. Working capital was \$128.5 million as of December 31, 1997, \$115.0 million lower than the \$243.5 million at year-end 1996. The ratio of current assets to current liabilities was 1.27 to 1 as of December 31, 1997, compared with 1.76 to 1 as of December 31, 1996. The ratio decreased from December 31, 1996, primarily due to accrued expenses for projected short-term asbestos-related liability payments and higher levels of short-term debt used to finance higher levels of receivables and inventories, refinancing of long-term debt and other general corporate purposes.

Cash from operations and uses of cash flow

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Net cash used for investing activities was \$152.8 million for the year ended December 31, 1997, down from \$239.8 million in 1996. This reduction was primarily due to lower purchases of property, plant and equipment and higher proceeds from the sale of land, facilities and other assets which were partially offset by additional acquisitions and investments in joint ventures, and higher investment in computer software.

Net cash used for financing activities was \$98.6 million for the year ended December 31, 1997, as cash provided by higher levels of short-term debt was offset by cash used for payment of dividends and reduction of long-term debt. In 1996, net cash used for financing activities was \$171.8 million as cash was used to reduce debt and redeem outstanding preferred stock in addition to the payment of dividends and repurchases of stock.

Under the 1994 and 1996 board-approved 5,500,000 common share repurchase plans, the company has repurchased approximately 3,661,000 shares through December 31, 1997, including 1,281,000 shares repurchased in 1997.

Long-term debt, excluding the company's guarantee of the ESOP loan, increased slightly in 1997. At December 31, 1997, long-term debt of \$223.1 million, or 16.7% of total capital, compared with \$219.4 million, or 17.4% of total capital, at the end of 1996. The 1997 and 1996 year-end ratios of total debt (including the company's financing of the ESOP loan) as a percent of total capital were 39.2% and 37.2%, respectively.

Other sources of capital include a \$300 million revolving line of credit, expiring 2001, which is used for general corporate purposes and as a backstop for commercial paper notes; and \$500 million of unissued debt and/or equity securities registered with the Securities and Exchange Commission. Should a need develop for additional financing, it is management's opinion that the company has sufficient financial strength to warrant the required support from lending institutions and financial markets. Early in 1998, the company's long-term debt rating was reduced by Standard & Poor's from A+ to A while Moody's remained at A2. The company's short-term debt ratings remained at A-1 from Standard & Poor's and P-1 from Moody's.

The company has increased its investment in computer software with projects to develop and implement a new corporate logistics system and a new financial and human resource system. These new systems are year-2000-compliant. In addition, a year 2000 project, expected to be completed in 1999, is converting the remainder of the company's systems to minimize this exposure. The costs of this project are not expected to be material to the company's results of operations, financial condition or liquidity. Since the company cannot yet be assured that suppliers and other third parties with which it does business will be compliant on a timely basis, the company cannot assess the potential impact, if any, that their noncompliance may have on the company.

The company is involved in significant asbestos-related litigation which is described more fully on pages 59-64 and which should be read in connection with this discussion and analysis. The company does not know how many claims will be filed against it in the future, or the details thereof, or of pending suits not fully reviewed, or the expense and any liability that may ultimately result therefrom, or whether an alternative to the Georgine settlement vehicle may emerge, or the ultimate liability if such alternative does not emerge, or the scope of its nonproducts insurance coverage ultimately deemed available.

The company has assessed the impact of the recent Supreme Court ruling on its projected asbestos resolution and defense costs. Subject to the uncertainties, limitations and other factors referred to above and based upon its experience, the company has recorded a current liability and long-term reserve totaling \$251.7 million on the balance sheet as an estimated minimum liability to defend and resolve probable and estimable asbestos-related personal injury claims currently pending and to be filed through 2003. This is management's best estimate of the minimum liability, although potential future costs for claims could range up to an additional \$387 million or an estimated maximum liability of approximately \$639 million. Because of the uncertainties related to asbestos litigation, it is not possible to estimate the number of personal injury claims that may be filed after 2003 or their cost. Therefore, the company's estimated liability does not reflect amounts for personal injury claims that may be filed after 2003, although it is likely there will be such additional claims. Management believes that the potential additional costs for claims to be filed through 2003 and those filed thereafter, net of any potential insurance recoveries, will not have a material after-tax effect on the financial condition of the company or its liquidity, although the net after-tax effect of any future liabilities recorded in excess of insurance assets could be material to earnings in a future period.

Total debt/total debt + equity

Funds from operations/total debt

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An insurance asset in the amount of \$291.6 million is recorded on the balance sheet and reflects the company's belief in the availability of insurance in this amount, based upon the company's success in insurance recoveries, the agreements, including the Wellington Agreement, that provide such coverage, the nonproducts recoveries by other companies and the opinion of outside counsel. Such insurance is probable of recovery through negotiation, alternative dispute resolution ("ADR") or litigation. A substantial portion of the insurance asset is in ADR, which the company believes will not be resolved until 1998 or later. As a consequence, a shortfall has developed between available insurance and amounts necessary for resolution and defense costs. This shortfall was \$39.9 million at the end of 1997 and included a \$1.5 million insurance recovery from an insolvent insurance carrier. The recovery of insurance assets to cover the shortfall will depend upon the resolution of the ADR and other disputes with the insurance carrier. The company does not believe that the after-tax effect of the shortfall will be material either to the financial condition of the company or to its liquidity.

Subject to the uncertainties, limitations and other factors referred to in the note covering asbestos-related legal proceedings, the company believes it is probable that substantially all of the expenses and any liability payments associated with the property damage claims will be paid under insurance coverage settlement agreements and through coverage from the outcome of the California insurance litigation. Even though uncertainties still remain as to the potential number of unasserted claims, liability resulting therefrom, and the ultimate scope of its insurance coverage, after consideration of the factors involved, including the Wellington Agreement and settlements with other insurance carriers, the results of the California insurance coverage litigation, the remaining reserve, the establishment of the Center, the likelihood that an alternative to the Georgine settlement will eventually emerge, and its experience, the company believes the asbestos-related claims against the company would not be material either to the financial condition of the company or to its liquidity, although as stated above, the net effect of any future liabilities recorded in excess of insurance assets could be material to earnings in such future period.

On June 16, 1997, the company commenced an all cash offer to purchase all of the outstanding common shares and common share equivalents (including convertible debentures and warrants on an as-if converted basis) of Domco Inc. ("Domco"), a Canadian subsidiary of Sommer Allibert, S.A. ("Sommer"). The offer has been extended and amended on a number of occasions since June, most recently to increase the bid price per common share to CDN \$26.50 (thereby increasing the aggregate proposed purchase price to CDN \$560 million) and to extend the expiration date of the offer to May 29, 1998. The extension is intended to permit the Quebec Securities Commission to rule on the issues of whether the merger of Tarkett AG ("Tarkett") with Sommer constitutes an indirect takeover of Domco and, if so, at a purchase price in excess of 115% of Domco's per share price without providing similar value to Domco's minority shareholders in violation of the rules under the Quebec Securities Act. The offer is conditional upon the valid tender of 51% of the outstanding common shares of Domco on a diluted basis. The company has recorded an asset of \$8.3 million for costs associated with the Domco acquisition. The company has obtained requisite regulatory approvals from the United States Federal Trade Commission, the Canadian Minister of Industry and the Competition Bureau in Canada. Sommer has stated that it does not intend to sell its shares of Domco to the company, and Domco's board of directors has rejected the company's offer to subscribe for Domco common shares.

On June 9, 1997, the company filed a complaint in the United States District Court for the Eastern District of Pennsylvania alleging that Sommer (subsequently amended to include Tarkett and Marc Assa, the President du Directoire of Sommer), had used confidential information provided by the company during negotiations regarding the purchase of Sommer's worldwide flooring assets to structure a transaction with Tarkett in violation of a confidentiality agreement and exclusivity understanding with the company and a duty to negotiate in good faith. The company intends to continue to pursue this litigation to recover damages in a trial scheduled to begin on September 15, 1998. The ultimate magnitude of the company's potential recovery is not known at this time.

On June 23, 1997, the company filed a claim, amended on August 11, 1997, in the Ontario Court (General Division) alleging that Sommer and its representatives on Domco's board breached their fiduciary duty to Domco and acted in a manner oppressive to Domco's minority shareholders when they rejected the company's bid for Domco. The company's motion requesting a court injunction to prevent the takeover of Domco by Tarkett, among other items, was dismissed. The company is continuing to pursue this litigation to recover damages from Sommer and Domco's directors, among other relief.

The company intends to continue to pursue all legal remedies available to it in the United States and Canada against Sommer, Domco's directors, Tarkett and Marc Assa.

MARKET RISK

The company uses financial instruments, including fixed and variable rate debt, as well as swap, forward and option contracts to finance its operations and to hedge interest rate, currency and commodity exposures. The swap, forward and option contracts are entered into for periods consistent with the underlying exposure and do not constitute positions independent of those exposures. The company does not enter into contracts for speculative purposes and is not a party to any leveraged instruments.

INTEREST RATE SENSITIVITY

The table below provides information about the company's debt obligations. The table presents principal cash flows and related weighted average interest rates by expected maturity dates. Weighted average variable rates are based on implied forward rates in the yield curve at the reporting date. The information is presented in US dollar equivalents, which is the company's reporting currency.

Expected maturity date (\$ millions)	1998	1999	2000	2001	2002	After 2002	Total
Liabilities							
Long-term debt:							
Fixed rate	\$ 13.5	\$ 21.0	\$ 22.1	\$ 7.5	\$ 0.0	\$ 153.0	\$ 217.1
Avg. interest rate	8.88%	4.79%	8.14%	9.00%	0.00%	9.13%	8.59%
Variable rate	\$ 1.0	\$ 4.0	\$ 5.0	\$ 2.0	\$ 0.0	\$ 8.5	\$ 20.5
Avg. interest rate	9.38%	8.28%	8.28%	8.28%	0.00%	3.90%	6.52%

The company is also party to forward starting interest rate swaps entered into in anticipation of future debt issuance. On December 31, 1997, the notional amount under these forward starting swaps was \$100.0 million with all swap initiation dates occurring during 1998. The market value of these forward agreements on December 31, 1997, was \$3.2 million less than the notional amount.

EXCHANGE RATE SENSITIVITY

The company uses foreign currency forward contracts and options to reduce the risk that future cash flows from transactions in foreign currencies will be negatively impacted by changes in exchange rates.

The table below provides anticipated net foreign cash flows for goods, services and financing transactions for the next 12 months.

Foreign currency exposure (\$ millions)	Commercial exposure	Financing exposure	Net hedge	Net position
British pound	\$(24.0)	\$(17.1)	\$ 12.1	\$(29.0)
Canadian dollar	37.0	--	--	37.0
French franc	(17.0)	3.3	(3.3)	(17.0)
German mark	(48.0)	12.4	(12.4)	(48.0)
Italian lira	25.0	2.3	(2.3)	25.0
Spanish peseta	7.0	2.3	(2.3)	7.0

Note 1: A positive amount indicates the company is a net receiver of this currency, while a negative amount indicates the company is a net payer.

Company policy allows hedges of cash flow exposures of up to one year. The table below summarizes the company's foreign currency forward contracts and average contract rates at December 31, 1997. Foreign currency amounts are translated at exchange rates as of December 31, 1997.

Foreign currency contracts (\$ millions)	Sold	Forward Contracts		
		Avg. rate	Bought	Avg. rate
British pound	\$ 5.0	\$ 1.68	\$17.1	1.61
Dutch guilder	2.0	2.00	--	--
French franc	3.3	5.9	--	--
German mark	12.4	1.79	--	--
Italian lira	2.3	1726	--	--
Spanish peseta	2.3	151.5	--	--

The foreign currency hedges are straightforward contracts that have no embedded options or other terms that involve a higher level of complexity or risk.

COMMODITY PRICE SENSITIVITY

The table below provides information about the company's natural gas swap contracts that are sensitive to changes in commodity prices. For the contracts, the table presents the notional amounts in millions of Btu's (MMBtu) and weighted average contract prices. All contracts mature in or before January 1999.

On Balance Sheet Commodity Related Derivatives	1998	1999	Total
Swap contracts (long)			
Contract amounts (MMBtu)	600,000	100,000	700,000
Weighted average price (\$/MMBtu)	\$2.26	\$2.43	\$2.29

CONSOLIDATED RESULTS

Net sales in 1997 of \$2.20 billion were 2.0% higher when compared with net sales of \$2.16 billion in 1996. Removing the currency translation impact of the stronger U.S. dollar, sales would have increased 3.6%. Added sales from the new Swedish flooring and soft-fiber ceilings joint ventures, along with sales growth in laminate flooring and the worldwide commercial and U.S. home center businesses, offset sales declines in the U.S. residential sheet flooring business.

Net earnings of \$185.0 million, or \$4.50 per diluted share compared with \$155.9 million, or \$3.61 per diluted share, in 1996. The increase is primarily related to the positive impact of manufacturing productivity improvements and some lower raw material costs in 1997 and to the negative impact of the 1996 charges for restructuring, floor discoloration product issues and the company's share of the extraordinary loss of Dal-Tile International Inc., in which the company had a 33% equity interest. Adversely affecting 1997 earnings were ceramic tile losses of \$42.4 million, or \$38.6 million after tax, including \$8.4 million, or \$6.1 million after tax, for the company's 34.4% share of operating losses incurred by Dal-Tile; an additional \$29.7 million before- and after-tax loss for the company's share of the charge incurred by Dal-Tile, primarily for uncollectible receivables and overstocked inventories; and \$4.3 million, or \$2.8 million after tax, for the amortization of Armstrong's initial investment in Dal-Tile over the underlying equity in net assets of the business combination. Net earnings in 1996 included after-tax charges of \$29.6 million for restructuring, or \$0.70 per diluted share; \$22.0 million for costs associated with the discoloration of a limited portion of flooring products, or \$0.53 per diluted share; and \$8.9 million, or \$0.21 per diluted share, for the company's share of an extraordinary loss from Dal-Tile.

The company's Economic Value Added (EVA) performance as measured by return on EVA capital of 13.3% in 1997 exceeded the company's 11% cost of capital by 2.3 percentage points. In 1996, the return on EVA capital was 14.8% and exceeded the company's 12% cost of capital by 2.8 percentage points. In 1997, the company's cost of capital was reduced to 11%, partially due to lower interest rates and stock price volatility.

Cost of goods sold in 1997 was 66.5% of sales, lower than the 67.7% in 1996 which included charges associated with a floor discoloration issue. Cost of goods sold was positively affected by continued productivity improvements and some lower raw material costs which offset some promotional pricing actions and a less favorable product mix.

Selling, general and administrative (SG&A) expenses in 1997 were \$385.3 million, or 17.5% of sales, which includes the currency translation impact of the stronger U.S. dollar and some lower advertising and administrative costs when compared with 1996. In 1996, SG&A expenses were \$413.2 million, or 19.2% of sales, and included a \$14.0 million nonrecurring charge for floor discoloration.

During 1996, the company learned that discoloration had occurred in a limited portion of its residential sheet flooring product lines. After correcting the manufacturing process to eliminate any further occurrence of this problem, the company recorded charges of \$34.0 million before tax, or \$22.0 million after tax (\$0.53 per diluted share), for associated inventory and claims costs.

In 1996, the company incurred restructuring charges of \$46.5 million, or \$29.6 million after tax (\$0.70 per diluted share), related primarily to reorganization of staff and plant positions, consolidation of the installation products businesses, restructuring of production processes and write-down of assets. Severance payments charged against restructuring reserves were \$17.2 million in 1997 relating to the elimination of 394 positions of which 247 terminations occurred since the beginning of 1997. As of December 31, 1997, an immaterial amount remained in the reserves for restructuring actions. Interest expense in 1997 of \$28.0 million was higher than 1996's interest expense of \$22.6 million. The primary reason for the increase was higher levels of short-term debt used to finance a variety of general corporate purposes.

The company's 1997 effective tax rate was 37.5%, negatively impacted by 3.4 percentage points from the recording of the company's equity share of the 1997 loss from Dal-Tile. The 1996 rate of 31.4% was positively affected by 1.7 percentage points from recording the company's equity share of the 1996 income from Dal-Tile.

GEOGRAPHIC AREA RESULTS (see page 8)

UNITED STATES

Net sales in 1997 were \$1.45 billion, higher than the \$1.42 billion recorded in 1996. Sales growth was strongest in the U.S. home center channel serviced through the Corporate Retail Accounts distribution unit, in the commercial flooring and ceilings businesses and in insulation products. These increases offset the negative impact of sales declines in U.S. residential sheet flooring.

Operating income in 1997 of \$236.1 million was higher than 1996's operating income of \$202.7 million. Cost reduction efforts, most notably in building products and insulation products, positively impacted 1997 operating income; however, this improvement was offset by the \$42.4 million loss from the ceramic tile segment (discussed on page 24). In 1996, operating income was negatively impacted by the previously mentioned charges of \$34.5 million for restructuring and \$34.0 million for floor discoloration issues.

Export sales of Armstrong products from the U.S. to trade customers of \$40.9 million increased \$6.9 million, or over 20% compared with 1996. The majority of the increase has come from a growth in sales to Latin America.

EUROPE

Sales and earnings results in the European markets remained mixed and year-to-year comparisons were negatively impacted by the currency translation effects of a stronger dollar. Net sales of \$545.6 million in 1997 decreased less than 1% with growth from recent product alliances, such as the Swedish flooring and ceilings joint ventures, and sales to Central and Eastern Europe, especially Russia, offset by the currency translation effects. Sales of industry products in our traditional market segments declined, reflecting competitive pricing and weakness in market economies in Western Europe, including the U.K. Operating income decreased less than 3% from 1996 with negative currency translation effects and small declines in floor coverings and building products somewhat offset by gains from significant cost reductions in industry products. Operating income in 1996 included \$11.0 million of restructuring charges.

OTHER FOREIGN

Net sales increased 6% from 1996 with growth occurring in insulation and building products which have both benefited from manufacturing facilities in China. Operating income decreased 14% in 1997, reflecting startup costs at the Shanghai ceiling plant earlier in 1997 and the more recent economic climate in other Southeast Asian countries.

Net trade sales

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INDUSTRY SEGMENT RESULTS (see page 3)

FLOOR COVERINGS

Worldwide floor coverings sales of \$1.12 billion increased 2.2% from \$1.09 billion in 1996 which included a \$14.1 million reduction for product returns for the potential discoloration of a limited portion of its product lines. The 1997 increase came primarily from the addition of sales from the laminate and Swedish joint venture product lines and higher sales in the U.S. commercial and home center channels. U.S. residential sheet flooring sales declined and were adversely affected by a general weakness in high-end professionally installed flooring, some shift toward alternative flooring products and consolidation of the wholesaler distribution channel.

Operating income of \$186.5 million compares to 1996's \$146.9 million which included charges of \$34.0 million associated with the discoloration issue and \$14.5 million for restructuring primarily related to the consolidation in the installation products business unit and other reorganizations in the floor products operations staff. Sales increases and productivity gains were more than offset by the negative impact of promotional pricing, a shift in product mix to more mid-priced residential sheet flooring and other lower margin products in the U.S. and start-up costs related to acquisitions and new product lines. Capital expenditures for property, plant and equipment in the floor coverings segment of \$76.6 million in 1997 were directed toward improving manufacturing processes. Capital expenditures in 1996 were \$117.7 million and were primarily related to the rollout of the Quest display and merchandising system and toward improved manufacturing process effectiveness.

Outlook

New products, including laminate flooring and those of the Swedish flooring joint venture, and sales of commercial and residential tile products should continue to be the drivers of sales growth in 1998. New strategies in the residential sheet flooring and laminate businesses will be focused on addressing changes in the end-use market for these products. Manufacturing margins should increase due to higher sales and lower costs resulting from the simplification of product structures and the manufacturing process. The margin increase should more than offset the higher advertising expense directed toward higher brand awareness. The home center channel, serviced through Corporate Retail Accounts, should continue to grow in 1998 at rates estimated to be greater than the overall home improvement category. Consolidation in the installation products business has been completed, and this business is now positioned to turn sales growth into solid returns.

BUILDING PRODUCTS

Net sales of \$754.5 million in the building products segment increased 5.0% from 1996. Sales growth was experienced in all geographic areas. In the Americas, strength came from the U.S. commercial market segment and Latin America. In Europe, added sales from the new Swedish soft-fiber ceilings joint venture and Eastern Europe offset the impact of sluggish Western European economies and continued lower selling prices. Sales grew in the Pacific Area (less than 10% of the segment's business); however, the economic slowdown in Southeast Asia in the latter part of 1997 has increased price competitiveness in this region.

Operating income of \$122.3 million increased 28.7% from 1996, which included \$8.3 million in restructuring charges. The major factors in the 1997 improvement were higher sales volume and increased productivity, reduced raw material prices and lower startup costs in China than in 1996. In addition, solid increases in profits continue to be realized from the WAVE grid joint venture. Negative factors somewhat reducing the improvement were competitive pricing actions in the U.S. home center channel and in Western Europe. In Eastern Europe and Russia, the increased sales are concentrated in lower margin products. Capital expenditures for property, plant and equipment were \$54.4 million compared with \$67.7 million in 1996.

Outlook

Business plans in this unit are directed toward heightened brand awareness, customer specific selling and training programs as well as focused efforts toward the most profitable products and channels. Continued growth is anticipated in commercial ceilings market segments in the U.S. and Latin America. In Europe, the results are expected to follow the same trend as 1997, with modest growth in the core Western European market and increased sales from the metal ceilings and Swedish soft-fiber ceilings alliances and Eastern Europe. The market in Asia is expected to continue to show growth although most of the Southeast Asian countries will be negatively affected for some time by the economic climate.

Operating income

[BAR CHART APPEARS HERE]

Capital additions

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INDUSTRY PRODUCTS

Worldwide industry products segment sales of \$328.2 million declined 5.2% when compared with 1996; however, without the translation impact of the stronger U.S. dollar, sales would have increased 2%. In the insulation products business sales declines from competitive market pressure in Europe were offset by increases in North America and the Pacific area. Sales of gasket products and textile products, the other two businesses in this segment, were slightly above 1996.

A record operating income of \$55.5 million increased \$15.4 million from 1996's \$40.1 million. The majority of the increase was related to productivity gains in insulation products in all geographic areas. Profits increased in gasket products due to the introduction of new products into European markets and an improved cost profile. The textile products business recorded a profit in 1997 compared with a loss in 1996. Capital expenditures for property, plant and equipment in the industry products segment were \$16.5 million compared with \$22.5 million in 1996.

Outlook

The European building industry is forecasted to remain soft in 1998. Competition due to overcapacity in the insulation products industry will continue to result in some price erosion; however, continued attention to lowering costs should counter the negative impact of competition. In Asia, the market for insulation products is expected to continue to expand although the economic climate in this area may affect results. Worldwide growth in gasket sales is anticipated, primarily due to new products with new applications.

CERAMIC TILE

The ceramic tile segment's 1997 operating loss of \$42.4 million included \$8.4 million for the company's share of operating losses incurred by Dal-Tile International Inc., in which the company has a 34.4% equity interest; an additional \$29.7 million after-tax loss for the company's share of the charge incurred by Dal-Tile, primarily for uncollectible receivables and overstocked inventories; and \$4.3 million for the amortization of Armstrong's initial investment in Dal-Tile over the underlying equity in net assets of the business combination. In 1996, the ceramic tile segment reported income of \$9.9 million.

Outlook

Major reorganization and restructuring efforts took place at Dal-Tile during 1997 to reduce overhead expenses and improve cash flow. Dal-Tile management anticipates that, in 1998, the business should return to earning a profit and be focused on improving customer service and increasing sales with the assistance of the new logistics system implemented in 1997. The company is evaluating all options regarding the Dal-Tile investment to ensure that the best interests of Armstrong's shareholders are served.

SUBSEQUENT EVENT

On February 25, 1998, the company filed a Form 13D/A with the Securities and Exchange Commission with respect to its ownership of Dal-Tile Common Stock stating that the company has concluded that its interests would be best served by disposing of its Dal-Tile investment. The company intends to pursue options available to it to sell its shares of Dal-Tile Common Stock either in a private transaction or through the public markets, though it is not precluding the possibility of acquiring additional shares should circumstances change in the future.

NEW ACCOUNTING PRONOUNCEMENTS

In June 1997, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 130, "Reporting Comprehensive Income." This statement requires that all items that are recognized under accounting standards as components of comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements.

In June 1997, the FASB issued SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." This statement establishes standards for reporting information about operating segments in annual financial statements and requires selected information about operating segments in interim financial reports issued to shareholders. It also establishes standards for related disclosures about products and services, geographic areas and major customers.

The company plans to adopt these accounting standards for periods beginning with January 1, 1998, as required. The adoption of these standards will not impact consolidated results, financial condition, or long-term liquidity.

FOURTH QUARTER 1997 COMPARED WITH FOURTH QUARTER 1996

Net sales of \$527.4 million were slightly lower than 1996's fourth-quarter sales of \$528.6 million. Sales would have increased 2.0% without the negative currency translation effect of a stronger U.S. dollar. Sales decreased in the floor coverings segment as strong sales in the U.S. residential flooring tile business unit and Europe, especially from the Swedish flooring joint venture, were more than offset by lower U.S. residential sheet flooring sales. Building products sales grew due to strength in the U.S. commercial market segment and added sales from the Swedish soft-fiber ceilings joint venture. Sales decreased in the industry products segment, largely due to a stronger U.S. dollar and competitive pricing in insulation products, particularly in Europe.

Operating income of \$72.2 million compares with \$79.4 million in the fourth-quarter 1996. By operating segment, increases were reported in the building products and industry products segments, while declines were reported in the floor coverings and ceramic tile segments. Operating income in the floor coverings segment of \$40.5 million decreased when compared with \$45.6 million in 1996. Sales increases in residential tile and commercial sheet and tile flooring were offset by promotional pricing and a shift in product mix to more mid-priced residential sheet flooring and other lower margin products. Fourth-quarter operating income for building products was \$28.8 million compared with 1996 fourth-quarter income of \$21.7 million. The significant factors driving this increase were sales growth, lower costs from productivity improvements and the increase in profits realized from the WAVE grid joint venture. Industry products operating income of \$13.9 million increased from \$9.9 million in the fourth quarter 1996. The increase resulted from lower manufacturing costs in the insulation, gasket and textile products business units.

The ceramic tile segment fourth-quarter operating loss of \$8.4 million represents Armstrong's share of the net loss of the Dal-Tile business combination and the amortization of the excess of the company's initial investment in Dal-Tile over the underlying equity in net assets. Fourth-quarter 1996 operating income of \$4.7 million reflects Armstrong's share of the after-tax operating income of Dal-Tile and the amortization of the excess of the company's initial investment in Dal-Tile over the underlying equity in net assets.

Cost of goods sold as a percent of sales was 67.6%, compared with 69.2% in the fourth quarter 1996. Lower raw material costs in floor coverings and building products, productivity improvements and controlled manufacturing period expense were the primary reasons for the lower manufacturing costs.

Armstrong's effective tax rate in fourth quarter 1997 was 31.3% and was comparable to the effective tax rate for continuing businesses of 31.4% in fourth quarter 1996.

Net earnings were \$46.8 million, or \$1.15 per diluted share and included losses of \$5.5 million after tax, or \$0.13 per diluted share, from the ceramic tile segment. These results compare with 1996's fourth-quarter net earnings of \$53.2 million or \$1.28 per diluted share, including \$4.2 million, or \$0.10 per diluted share, of earnings from the company's investment in Dal-Tile.

1996 COMPARED WITH 1995

FINANCIAL CONDITION

As shown on the Consolidated Statements of Cash Flows (see page 33), net cash provided by operating activities and the sale of assets was sufficient to cover normal working capital requirements, payments related to restructuring activities and additional investment in plant, property and equipment. Most of the 1996 beginning cash balance plus proceeds from exercised stock options covered the reduction of debt, payments of dividends, preferred stock redemptions, repurchase of shares, purchase of computer software and additional investment in Dal-Tile International Inc. The beginning cash balance of \$256.9 million included proceeds from the sale of Thomasville Furniture Industries, Inc., in December 1995.

Working capital was \$243.5 million as of December 31, 1996, \$103.3 million lower than the \$346.8 million reported at year-end 1995. The reduction in working capital over 12 months resulted primarily from the \$191.5 million decrease in cash. Partially offsetting the working capital decrease were increases in inventories of \$10.2 million, income tax benefits of \$22.5 million, the \$33.9 million decrease in short-term debt and current installments of long-term debt and the \$24.1 million decrease in accounts payable and accrued expenses.

The ratio of current assets to current liabilities was 1.76 to 1 as of December 31, 1996, compared with 1.92 to 1 as of December 31, 1995, primarily due to the reduced levels of cash.

On October 1, 1996, the Employee Stock Ownership Plan (ESOP) and the Retirement Savings Plan (RSP) were merged to form the new Retirement Savings and Stock Ownership Plan (RSSOP). Prior to the merger of the plans, on July 31, the trustee of the ESOP converted the preferred stock held by the trust into approximately 5.1 million shares of common stock with a book value of \$139.1 million at a one-for-one ratio.

Long-term debt, excluding the company's guarantee of the ESOP loan, increased \$31.1 million in 1996. The increase was primarily due to a low interest rate loan for a capital addition at the Kankakee, Illinois, floor tile plant. At December 31, 1996, long-term debt of \$219.4 million represented 17.4% of total capital compared with 14.9% at the end of 1995. The 1996 and 1995 year-end ratios of total debt (including the company's financing of the ESOP loan) as a percent of total capital were 37.2% and 38.5%, respectively.

In July 1996, the Board of Directors authorized the company to repurchase 3.0 million shares of its common stock (in addition to the 2.5 million shares authorized in 1994), through the open market or through privately negotiated transactions, bringing the total authorized common share repurchases to 5.5 million shares. The increased stock repurchase authorization will allow greater flexibility in deploying cash flow and, to the extent that shares can be repurchased at attractive prices, should increase earnings per share. Since the inception of the plan, the company repurchased approximately 2,380,000 shares through December 31, 1996, including approximately 1,328,000 shares repurchased in 1996. In addition to shares repurchased under the above plan, approximately 364,600 ESOP shares were repurchased in 1996.

Capital in excess of par value increased \$112.8 million from December 31, 1995, primarily as a result of two transactions. First, the company reissued treasury stock to the trustee of the ESOP in the conversion of the preferred stock held by the trust as mentioned above. Capital in excess of par value increased \$102.4 million representing the excess of conversion value of the ESOP convertible shares over the average acquisition cost of the treasury shares. Second, Dal-Tile issued new shares in a public offering in August and used part of the proceeds from the public offering to refinance all of its existing debt. Although Armstrong's ownership share declined to 33% from 37%, Dal-Tile's net assets increased, adding to the overall carrying value of Armstrong's investment and resulting in the company recording \$14.5 million as additional capital in excess of par value.

CONSOLIDATED RESULTS

Net sales of \$2.16 billion were lower when compared with 1995's net sales of \$2.33 billion which included \$0.24 billion of sales from the ceramic tile operations. Beginning in 1996, ceramic tile was reported on the equity method; therefore, a year-to-year sales comparison cannot be made for this industry segment. Sales growth occurred in the floor coverings and building products segments. The floor coverings segment sales growth came primarily from residential and commercial floor tile sold through the U.S. home center channel and floor sales in Eastern Europe and Russia. In the building products segment, strong commercial ceiling sales in the latter part of the year offset earlier servicing problems resulting from severe weather conditions in the first quarter 1996. Industry products sales were adversely affected by competitive pressure in European insulation products and lower global textile products sales which more than offset the positive impact of increases in the gasket and specialty paper business.

Earnings from continuing businesses after income taxes in 1996 were \$164.8 million or \$4.04 per basic share and \$3.82 per diluted share and included after-tax charges of \$29.6 million for restructuring and \$22.0 million for costs associated with the discoloration of a limited portion of flooring products. Earnings from continuing businesses after income taxes in 1995 were \$13.6 million and included a \$46.6 million charge after tax for restructuring and a loss of \$116.8 million after tax related to the business combination of Armstrong's ceramic tile operations with Dal-Tile.

Net earnings for 1996 were \$155.9 million, or \$3.81 per basic share and \$3.61 per diluted share and included the restructuring and discoloration charges mentioned above plus \$8.9 million or \$0.21 per diluted share for the company's portion of an extraordinary loss from Dal-Tile related to the refinancing of Dal-Tile's outstanding debt. Net earnings in 1995 were \$123.3 million or \$2.94 per basic share and \$2.68 per diluted share and included \$25.8 million of after-tax earnings from the discontinued operations of Thomasville Furniture Industries, Inc., and \$83.9 million representing the after-tax gain from its sale.

The company's Economic Value Added (EVA) performance as measured by return on EVA capital was 14.8% in 1996, exceeding 1995's return on EVA capital of 14.0% and the company's 12% cost of capital.

Cost of goods sold in 1996 was 67.7% of sales, slightly lower than the 68.0% recorded in 1995. The 1996 cost of goods sold included \$5.9 million for charges associated with the floor discoloration issue which were offset by lower raw material and other manufacturing costs. The cost of goods sold in 1995 included the impact of start-up costs of approximately \$3.1 million related to the insulation products facility in Mebane, North Carolina.

Selling, general and administrative (SG&A) expenses in 1996 were \$413.2 million which included \$14.0 million of expenses related to the discoloration issue. In 1995, SG&A expenses were \$457.0 million and included \$59.9 million of SG&A expenses of the ceramic tile operations which was reported on an equity basis in 1996.

The second-quarter 1996 before-tax restructuring charge for continuing businesses of \$46.5 million, or \$29.6 million after tax (\$0.79 per basic share and \$0.70 per share on a diluted basis), related primarily to the reorganization of corporate and business unit staff positions; realignment and consolidation of the Armstrong and W.W. Henry installation products businesses; restructuring of production processes in the Munster, Germany, ceilings facility; early retirement opportunities for employees in the Fulton, New York, gasket and specialty paper products facility; and write-down of assets. These actions affected approximately 500 employees, about two-thirds of whom were in staff positions. These restructuring actions continued the company's ongoing efforts to streamline the organization and enable the businesses to be the best-cost suppliers in their markets. The charges were estimated to be evenly split between cash payments and noncash charges. The majority of the cash outflow was expected to occur over 12 months. It was anticipated that ongoing cost reductions and productivity improvements should permit recovery of the charges in less than two years. In 1995, restructuring charges of \$71.8 million before tax or \$46.6 million after tax (\$1.09 per share on a diluted basis) were recorded. These charges related primarily to the closure of a plant in Braintree, Massachusetts, and for severance and early retirement incentives for approximately 670 employees in the North American resilient flooring business and the European industry products and building products businesses.

Actual severance payments charged against restructuring reserves were \$32.1 million in 1996 relating to the elimination of 724 positions, of which 323 terminations occurred since the beginning of 1996. As of December 31, 1996, \$50.3 million of reserves remained for restructuring actions.

In July 1996, the company learned that discoloration in a limited portion of its residential sheet flooring product lines was occurring. The problem was traced to a raw material used in production primarily between September 1995 and July 1996. The manufacturing process was corrected to eliminate any further occurrence of this problem. New production was shipped to customers to meet demand for this product. A portion of the production of the affected product lines was shipped to retailers and potentially installed in consumers' homes. The remainder was in the company's, wholesalers' or retailers' inventory.

In September 1996, the company recorded charges of \$34.0 million before tax or \$22.0 million after tax (\$0.53 per diluted share) for costs associated with the discoloration issue. These charges included the write-down to realizable value of the company's inventory on hand or to be returned from independent wholesalers and the potential cost of removing and replacing discolored product installed in consumers' homes. The company planned to continue to monitor claims levels associated with these products and make any further adjustments in the reserve based on experience.

Interest expense in 1996 of \$22.6 million was lower than 1995's interest expense of \$34.0 million. The primary reasons for the decrease were the lower levels of short-term debt and lower interest expense requirements on long-term debt.

Armstrong's effective tax rate for continuing businesses in 1996 was 31.4%. In 1995, Armstrong's effective tax benefit for continuing businesses was 65.9%. Removing the tax effects of the loss on the ceramic tile business combination, the effective tax rate would have been 29.7%, reflecting tax benefits related to reduced foreign and state income tax expense.

GEOGRAPHIC AREA RESULTS (see page 8)

UNITED STATES

Net sales in 1996 were \$1.42 billion, slightly lower than the \$1.59 billion recorded in 1995 which included \$0.24 billion of ceramic tile sales. Sales through the home center channel had significant year-to-year increases. The commercial markets for ceilings and the residential and commercial markets for floor tile continue to show strength. U.S. residential sheet flooring sales were slightly below 1995. Operating income of \$202.7 million was higher than 1995's operating income of \$7.7 million which included a \$177.2 million loss due to the ceramic tile business combination. An organizational effectiveness study to review the company's staff support activities was implemented by late 1996, and the restructuring activities associated with this study had an adverse impact on operating income of \$34.5 million before tax. Operating income was also negatively affected by the one-time charge of \$34.0 million related to the floor discoloration issue mentioned above. Restructuring activities in 1995 resulted in \$45.5 million before tax charged against operating income. Operating income for 1996 was positively impacted by higher sales levels in the floor coverings and building products segments and was leveraged through ongoing cost reduction efforts. Export sales of Armstrong products from the U.S. to trade customers of \$34.0 million increased nearly \$1.9 million, or 6.1%, compared with 1995.

EUROPE

Sales in 1996 by the European affiliates reflected the soft economy largely offset by the ability to enter into new market areas such as Eastern Europe and Russia. Net sales decreased 1.8% to \$548.4 million compared with 1995. Insulation sales were negatively impacted by competitive pressures, although they increased in the latter half of 1996. Floor Products sales increased from 1995, setting several quarterly sales records in 1996. Building Products sales increased slightly, despite softened demand and competitive pressure in the Western European commercial market segment. Operating income increased 26.8% over 1995, primarily due to cost savings obtained from prior years' restructuring activities. Restructuring charges in Europe were \$11.0 million and \$24.9 million in 1996 and 1995, respectively. In floor products, increased volume in addition to productivity improvements have resulted in improved profits in the residential sheet business. European insulation products operating income has been positively impacted by its continued efforts to be the best-cost supplier in the industry.

OTHER FOREIGN

Sales increased 4.9% over 1995, with ceiling sales in the Pacific Rim providing a significant part of the growth. Sales growth in Latin America for Building Products continues a trend established over the past three years. Operating income increased 28.6% over 1995, with start-up costs for the new ceilings plant in China totaling \$3.8 million offset by lower costs in the Pacific area Floor Products and Building Products Operations.

INDUSTRY SEGMENT RESULTS (see page 3)

FLOOR COVERINGS

In the floor coverings segment, 1996 net sales of \$1.09 billion were slightly above 1995's \$1.05 billion and included a reduction of \$14.1 million for customer returns associated with the discoloration of a limited portion of its Residential Inlaid Color Sheet Flooring products line. The adverse effect of these returns and the small decline in the U.S. residential sheet business were offset by increases in residential sheet flooring sales in Europe, especially Eastern Europe and Russia, and sales of all products to U.S. home centers. In the home center channel, which is serviced through the Corporate Retail Accounts Division, the strategy of segmenting products for the home centers proved to be successful. Laminate flooring, manufactured and marketed in alliance with the F. Egger Company of Austria, had a good initial market reaction. Operating income included a \$34.0 million charge associated with the discoloration issue and a \$14.5 million restructuring charge primarily related to the consolidation of the separate Armstrong and W.W. Henry installation products businesses and to other reorganizations in the floor products operations staff. Operating income in 1995 included a restructuring charge of \$25.0 million primarily related to the elimination of positions in North America. Records were set in 1996 in both the U.S. residential and commercial tile businesses. Lower raw material costs and increased manufacturing productivity had a positive impact on the cost profile of this business. However, operating income was adversely impacted by start-up costs for laminate flooring. Capital expenditures in this segment increased \$40.4 million to \$117.7 million and were directed toward the rollout of the Quest display and merchandising system and toward improved manufacturing process effectiveness.

BUILDING PRODUCTS

In the building products segment, net sales of \$718.4 million in 1996 increased more than 5.3% when compared to 1995 with growth primarily in North America and the Pacific Rim. North American sales increased significantly with the major areas of market strength in the commercial market segment and the home center channel. Manufacturing recovered from the severe weather conditions of early 1996, while inventories and service levels stabilized in anticipation of sales growth in 1997. Operating income increased to \$95.1 million, 3.1% over 1995. Operating income in 1996 included an \$8.3 million restructuring charge, the majority of which related to simplifying production processes in the Munster, Germany, ceilings facility. The balance of the restructuring charge was associated with staff reorganizations and asset write-downs in Europe. In 1995, operating income was adversely impacted by a \$6.3 million restructuring charge, primarily related to elimination of administrative functions in the European operations. In the earlier part of 1996, operating income had been adversely impacted by weather-related problems in North America and Europe. During 1996, additional costs were incurred for integration and start-up of the new metal ceilings products business and the wet-formed ceiling products plant in China. However, higher sales volume in 1996, improvements in its production processes and reductions in its nonmanufacturing expenses more than offset these additional costs. Capital expenditures in this segment increased by \$18.5 million to \$67.7 million. Excellent profit growth continued from WAVE, the grid system joint venture with Worthington Industries.

INDUSTRY PRODUCTS

Sales for the industry products segment of \$346.2 million in 1996 decreased less than 1% when compared with 1995 sales of \$348.8 million. Sales in 1995 included \$7.9 million of an exchange translation benefit when compared to 1996 rates and \$4.9 million from the champagne cork business divested in 1995. Operating income for 1996 was \$40.1 million and includes a \$4.0 million restructuring charge, the majority of which related to an early retirement offering to employees of the Fulton, New York, gasket and specialty paper products facility. Operating income in 1995 of \$9.3 million included a \$31.4 million restructuring charge related to the closing of the Braintree, Massachusetts, plant and elimination of employee positions in Europe. For insulation products, cost reductions in Europe enabled the business to remain competitive through lower selling prices and thus to continue to gain market share, while in the U.S. sales growth was achieved through increased market share. As a result of these strategies, operating income for insulation products increased. Income increased significantly for Armstrong Industrial Specialties, Inc., especially in its gaskets business. The textile products business continues to implement several cost-saving initiatives to reduce its overhead. Despite these changes, the business continued to generate a small operating loss of approximately \$3.0 million due to continued worldwide market softness in the textile industry. Capital expenditures in the industry products segment decreased \$22.5 million from the higher levels of 1995 when expenditures were made for the construction of two plants and for the acquisition of another plant.

CERAMIC TILE

In the ceramic tile segment, 1996 results represent the company's share of the after-tax net income of the Dal-Tile business combination reduced by the amortization of the excess of the company's initial investment in Dal-Tile over the underlying equity in net assets. Operating income for 1995 reflected the pretax operating income of the ceramic tile operations, primarily the American Olean Tile Company. Dal-Tile took several initiatives during 1996 to integrate the business, including the closure of two plants and numerous sales service centers. Sales growth in 1996 for ceramic tile occurred primarily in the home center and independent distributor channels.

Item 7A. Quantitative and Qualitative Disclosure About Market Risk

(See pages 20 to 21 under Item 7 above.)

Item 8. Financial Statements and Supplementary Data

Quarterly Financial Information

Quarterly financial information (millions except for per-share data)		First	Second	Third	Fourth	Total year
1997	Net sales	\$518.3	\$577.4	\$575.6	\$527.4	\$2,198.7
	Gross profit	171.3	199.2	195.6	170.9	737.0
	Net earnings	45.5	58.9	33.8	46.8	185.0
	Per share of common stock:					
	Basic: Net earnings	1.11	1.45	0.83	1.16	4.55
	Diluted: Net earnings	1.10	1.43	0.82	1.15	4.50
	Dividends per share of common stock	0.40	0.44	0.44	0.44	1.72
	Price range of common stock--high	72 1/4	75 1/4	74 9/16	75 3/8	75 3/8
	Price range of common stock--low	64 3/4	61 1/2	64 3/8	64 1/8	61 1/2
1996	Net sales	\$501.2	\$563.2	\$563.4	\$528.6	\$2,156.4
	Gross profit	156.7	198.4	178.4	163.0	696.5
	Earnings before extraordinary loss	36.3	30.6	44.2	53.7	164.8
	Net earnings	36.3	30.6	35.8	53.2	155.9
	Per share of common stock:*					
	Basic: Earnings before extraordinary loss	0.89	0.74	1.07	1.30	4.04
	Net earnings	0.89	0.74	0.87	1.29	3.81
	Diluted: Earnings before extraordinary loss	0.81	0.68	1.06	1.29	3.82
	Net earnings	0.81	0.68	0.86	1.28	3.61
	Dividends per share of common stock	0.36	0.40	0.40	0.40	1.56
	Price range of common stock--high	64 1/2	61 5/8	65 1/2	75 1/4	75 1/4
	Price range of common stock--low	57 7/8	53 1/2	51 7/8	61 3/4	51 7/8

*The sum of the quarterly earnings per-share data does not equal the total year amounts due to changes in the average shares outstanding and, for diluted data, the exclusion of the antidilutive effect in certain quarters.

CONSOLIDATED STATEMENTS OF EARNINGS

Millions except for per-share data	Years ended December 31		
	1997	1996	1995
Net sales	\$ 2,198.7	\$ 2,156.4	\$ 2,325.0
Cost of goods sold	1,461.7	1,459.9	1,581.1
Gross profit	737.0	696.5	743.9
Selling, general and administrative expenses	385.3	413.2	457.0
Equity (earnings) loss from affiliates	29.7	(19.1)	(6.2)
Restructuring charges	--	46.5	71.8
Loss from ceramic tile business combination	--	--	177.2
Operating income	322.0	255.9	44.1
Interest expense	28.0	22.6	34.0
Other expense (income), net	(2.2)	(6.9)	1.9
Earnings from continuing businesses before income taxes	296.2	240.2	8.2
Income taxes	111.2	75.4	(5.4)
Earnings from continuing businesses	185.0	164.8	13.6
Discontinued business:			
Earnings from operations of Thomasville Furniture Industries, Inc. (less income taxes of \$13.9)	--	--	25.8
Gain on disposal of discontinued business (less income taxes of \$53.4)	--	--	83.9
Earnings before extraordinary loss	185.0	164.8	123.3
Extraordinary loss (less income taxes of \$0.7)	--	(8.9)	--
Net earnings	\$ 185.0	\$ 155.9	\$ 123.3
Dividends paid on Series A convertible preferred stock	--	8.8	18.8
Tax benefit on dividends paid on unallocated preferred shares	--	2.0	4.5
Net earnings applicable to common stock	\$ 185.0	\$ 149.1	\$ 109.0
Per share of common stock (see note on page 35):			
Basic:			
Earnings (loss) from continuing businesses	\$ 4.55	\$ 4.04	\$ (0.02)
Earnings from discontinued business	--	--	0.70
Gain on sale of discontinued business	--	--	2.26
Earnings before extraordinary loss	4.55	4.04	2.94
Extraordinary loss	--	(0.23)	--
Net earnings	\$ 4.55	\$ 3.81	\$ 2.94
Diluted:			
Earnings (loss) from continuing businesses	\$ 4.50	\$ 3.82	\$ (0.02)
Earnings from discontinued business	--	--	0.60
Gain on sale of discontinued business	--	--	1.96
Earnings before extraordinary loss	4.50	3.82	2.68
Extraordinary loss	--	(0.21)	--
Net earnings	\$ 4.50	\$ 3.61	\$ 2.68

The Notes to Consolidated Financial Statements, pages 35-64, are an integral part of these statements.

CONSOLIDATED BALANCE SHEETS

Millions except for numbers of shares and per-share data	As of December 31	1997	1996
Assets			
Current assets:			
Cash and cash equivalents	\$	57.9	\$ 65.4
Accounts and notes receivable (less allowance for discounts and losses: 1997--\$37.5; 1996--\$34.9)		252.6	216.7
Inventories		220.1	205.7
Income tax benefits		25.9	49.4
Other current assets		43.5	27.3
Total current assets		600.0	564.5
Property, plant and equipment (less accumulated depreciation and amortization: 1997--\$1,004.3; 1996--\$974.9)		972.2	964.0
Insurance for asbestos-related liabilities		291.6	141.6
Investment in affiliates		174.9	204.3
Other noncurrent assets		336.8	261.2
Total assets	\$	2,375.5	\$ 2,135.6
Liabilities and shareholders' equity			
Current liabilities:			
Short-term debt	\$	84.1	\$ 14.5
Current installments of long-term debt		14.5	13.7
Accounts payable and accrued expenses		339.9	273.3
Income taxes		33.0	19.5
Total current liabilities		471.5	321.0
Long-term debt		223.1	219.4
Employee Stock Ownership Plan (ESOP) loan guarantee		201.8	221.3
Deferred income taxes		53.7	30.5
Postretirement and postemployment benefit liabilities		248.0	247.6
Asbestos-related long-term liabilities		179.7	141.6
Other long-term liabilities		172.1	151.9
Minority interest in subsidiaries		15.0	12.3
Total noncurrent liabilities		1,093.4	1,024.6
Shareholders' equity:			
Common stock, \$1 par value per share			
Authorized 200 million shares; issued 51,878,910 shares		51.9	51.9
Capital in excess of par value		155.1	162.1
Reduction for ESOP loan guarantee		(207.7)	(217.4)
Retained earnings		1,339.6	1,222.6
Foreign currency translation		(1.8)	17.3
		1,337.1	1,236.5
Less common stock in treasury, at cost:			
1997--11,759,510 shares; 1996--10,714,572 shares		526.5	446.5
Total shareholders' equity		810.6	790.0
Total liabilities and shareholders' equity	\$	2,375.5	\$ 2,135.6

The Notes to Consolidated Financial Statements, pages 35-64, are an integral part of these statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Millions	Years ended December 31	1997	1996	1995
Cash flows from operating activities:				
Net earnings		\$185.0	\$155.9	\$123.3
Adjustments to reconcile net earnings to net cash provided by operating activities:				
Depreciation and amortization excluding discontinued business		132.7	123.7	123.1
Depreciation and amortization for discontinued business		--	--	13.0
Deferred income taxes		24.2	11.2	(8.7)
Equity change in affiliates		37.2	(18.2)	(6.3)
Gain on sale of discontinued businesses		--	--	(83.9)
Loss on ceramic tile business combination net of taxes		--	--	116.8
Loss from restructuring activities		--	46.5	71.8
Restructuring payments		(18.6)	(37.4)	(18.3)
Payments for asbestos-related claims		(41.4)	--	--
Extraordinary loss		--	8.9	--
Changes in operating assets and liabilities net of effect of discontinued business, restructuring and dispositions:				
(Increase) decrease in receivables		(40.8)	3.6	6.9
(Increase) in inventories		(12.8)	(11.5)	(34.3)
(Increase) decrease in other current assets		10.5	(22.8)	9.8
(Increase) in other noncurrent assets		(69.0)	(57.4)	(23.4)
Increase (decrease) in accounts payable and accrued expenses		16.6	(3.2)	(37.0)
Increase (decrease) in income taxes payable		11.5	2.5	(8.2)
Increase in other long-term liabilities		23.2	15.2	20.0
Other, net		(11.7)	3.9	5.4
Net cash provided by operating activities		246.6	220.9	270.0
Cash flows from investing activities:				
Purchases of property, plant and equipment excluding discontinued business		(141.7)	(220.7)	(171.8)
Purchases of property, plant and equipment for discontinued business		--	--	(14.3)
Investment in computer software		(18.8)	(7.3)	(10.9)
Proceeds from sale of land, facilities and discontinued businesses		24.3	3.6	342.6
Acquisitions		(4.2)	--	(20.7)
Investment in affiliates		(12.4)	(15.4)	(27.6)
Net cash provided by (used for) investing activities		(152.8)	(239.8)	97.3
Cash flows from financing activities:				
Increase (decrease) in short-term debt		69.3	(7.1)	3.2
Issuance of long-term debt		7.2	40.8	--
Reduction of long-term debt		(17.0)	(40.0)	(20.1)
Cash dividends paid		(70.0)	(70.1)	(70.8)
Purchase of common stock for the treasury, net		(89.2)	(81.5)	(41.3)
Preferred stock redemption		--	(21.4)	(2.9)
Proceeds from exercised stock options		7.9	6.2	7.0
Other, net		(6.8)	1.3	2.3
Net cash used for financing activities		(98.6)	(171.8)	(122.6)
Effect of exchange rate changes on cash and cash equivalents		(2.7)	(0.8)	0.2
Net increase (decrease) in cash and cash equivalents		\$ (7.5)	\$ (191.5)	\$ 244.9
Cash and cash equivalents at beginning of year		\$ 65.4	\$ 256.9	\$ 12.0
Cash and cash equivalents at end of year		\$ 57.9	\$ 65.4	\$ 256.9
Supplemental cash flow information				
Interest paid		\$ 23.5	\$ 20.7	\$ 29.6
Income taxes paid		\$ 54.5	\$ 65.5	\$ 76.9

The Notes to Consolidated Financial Statements, pages 35-64, are an integral part of these statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Millions except for per-share data	Years ended December 31		
	1997	1996	1995
Series A convertible preferred stock:			
Balance at beginning of year	\$ --	\$ 258.9	\$ 261.6
Conversion of preferred stock to common	--	(241.5)	--
Shares retired	--	(17.4)	(2.7)
Balance at end of year	\$ --	\$ --	\$ 258.9
Common stock, \$1 par value:			
Balance at beginning and end of year	\$ 51.9	\$ 51.9	\$ 51.9
Capital in excess of par value:			
Balance at beginning of year	\$ 162.1	\$ 49.3	\$ 39.3
Gain in investment in affiliates	--	14.5	--
Minimum pension liability adjustments	(4.5)	(7.4)	--
Conversion of preferred stock to common	--	102.4	--
Stock issuances and other	(2.5)	3.3	10.0
Balance at end of year	\$ 155.1	\$ 162.1	\$ 49.3
Reduction for ESOP loan guarantee:			
Balance at beginning of year	\$ (217.4)	\$ (225.1)	\$ (233.9)
Principal paid	19.6	13.4	10.7
Loans to ESOP	(5.5)	(4.2)	--
Accrued compensation	(4.4)	(1.5)	(1.9)
Balance at end of year	\$ (207.7)	\$ (217.4)	\$ (225.1)
Retained earnings:			
Balance at beginning of year	\$1,222.6	\$1,133.8	\$1,076.8
Net earnings for year	185.0	155.9	123.3
Tax benefit on dividends paid on unallocated common shares	2.0	1.0	--
Tax benefit on dividends paid on unallocated preferred shares	--	2.0	4.5
Total	\$1,409.6	\$1,292.7	\$1,204.6
Less dividends:			
Preferred stock	\$ --	\$ 8.9	\$ 18.8
Common stock			
\$1.72 per share in 1997;	70.0		
\$1.56 per share in 1996;		61.2	
\$1.40 per share in 1995			52.0
Total dividends	\$ 70.0	\$ 70.1	\$ 70.8
Balance at end of year	\$1,339.6	\$1,222.6	\$1,133.8
Foreign currency translation:			
Balance at beginning of year	\$ 17.3	\$ 18.0	\$ 8.3
Translation adjustments and hedging activities	(18.2)	(4.4)	10.9
Allocated income taxes	(0.9)	3.7	(1.2)
Balance at end of year	\$ (1.8)	\$ 17.3	\$ 18.0
Less treasury stock at cost:			
Balance at beginning of year	\$ 446.5	\$ 511.8	\$ 468.9
Stock purchases	89.2	81.5	41.3
Conversion of preferred stock to common	--	(139.1)	--
Stock issuance activity, net	(9.2)	(7.7)	1.6
Balance at end of year	\$ 526.5	\$ 446.5	\$ 511.8
Total shareholders' equity	\$ 810.6	\$ 790.0	\$ 775.0

The Notes to Consolidated Financial Statements, pages 35-64, are an integral part of these statements.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates. These financial statements are prepared in accordance with generally accepted accounting principles and include management estimates and judgments, where appropriate. Actual results may differ from these estimates.

Consolidation Policy. The consolidated financial statements and accompanying data in this report include the accounts of the parent Armstrong World Industries, Inc., and its domestic and foreign subsidiaries. All significant intercompany transactions have been eliminated from the consolidated statements.

Earnings per Common Share. In 1997, the company adopted Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings per Share." The adoption of this statement requires the company to replace primary and fully diluted earnings per share with basic and diluted earnings per share. Basic earnings per share are computed by dividing the earnings available to common shareholders by the weighted average number of shares of common stock outstanding during the year. Diluted earnings per common share reflects the potential dilution of securities that could share in the earnings. (See note on page 41.)

Advertising Costs. The company's practice is to expense the costs of advertising as they are incurred.

Postretirement Benefits. The company has plans that provide for medical and life insurance benefits to certain eligible employees when they retire from active service. Generally, the company's practice is to fund the actuarially determined current service costs and the amounts necessary to amortize prior service obligations over periods ranging up to 30 years, but not in excess of the full funding limitations.

Taxes. Deferred tax assets and liabilities are recognized using enacted tax rates for expected future tax consequences of events recognized in the financial statements or tax returns. The tax benefit for dividends paid on unallocated shares of preferred stock held by the ESOP was recognized in shareholders' equity.

Cash and Cash Equivalents. Short-term investments, substantially all of which have maturities of three months or less when purchased, are considered to be cash equivalents and are carried at the lower of cost or an amount generally approximating market value.

Inventories. Inventories are valued at the lower of cost or market. Approximately 57% of 1997's inventories are valued using the last in, first out (LIFO) method. Other inventories are generally determined on a first in, first out (FIFO) method.

Long-Lived Assets. Property, plant and equipment values are stated at acquisition cost, with accumulated depreciation and amortization deducted to arrive at net book value. Depreciation charges for financial reporting purposes are determined generally on the straight-line basis at rates calculated to provide for the retirement of assets at the end of their useful lives. Accelerated depreciation is generally used for tax purposes. Impairment losses are recorded when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. When assets are disposed of or retired, their costs and related depreciation are removed from the books, and any resulting gains or losses are reflected in "Selling, general and administrative expenses."

Costs of the construction of certain long-term assets include capitalized interest which is amortized over the estimated useful life of the related asset.

Goodwill and Other Intangibles. Goodwill and other intangibles are amortized on a straight-line basis over periods up to 30 years. On a periodic basis, the company estimates the future undiscounted cash flows of the businesses to which goodwill relates in order to ensure that the carrying value of goodwill has not been impaired.

Financial Instruments. The company uses financial instruments to diversify or offset the effect of currency and interest rate variability.

The company may enter into foreign currency forward contracts and options to offset the effect of exchange rate changes on cash flow exposures denominated in foreign currencies. The exposures include firm commitments and anticipated events encompassing sales, royalties, service fees, dividends and intercompany loans.

Realized and unrealized gains and losses on contracts are marked to market and recognized in the consolidated statements of earnings. Unrealized gains and losses on foreign currency options (which consist primarily of purchased options that are designated as effective hedges) as well as option premium expense are deferred and included in the statements of earnings as part of the underlying transactions. Realized and unrealized gains and losses on foreign currency contracts used to hedge intercompany transactions having the character of long-term investments are included in the foreign currency translation component of shareholders' equity.

The company may enter into interest rate swap agreements to alter the interest rate risk profile of outstanding debt, thus altering the company's exposure to changes in interest rates. In these swaps, the company agrees to exchange, at specified intervals, the difference between fixed and variable interest amounts calculated by reference to a notional principal amount. Any differences paid or received on interest rate swap agreements are recognized as adjustments to interest rate expense over the life of the swap.

The company continuously monitors developments in the capital markets and only enters into currency and swap transactions with established counterparties having investment-grade ratings. The exposure to individual counterparties is limited, and thus the company considers the risk of counterparty default to be negligible.

NATURE OF OPERATIONS

INDUSTRY SEGMENTS

at December 31 (millions)	1997	1996	1995
Net trade sales:			
Floor coverings	\$1,116.0	\$1,091.8	\$1,053.9
Building products	754.5	718.4	682.2
Industry products	328.2	346.2	348.8
Ceramic tile	--	--	240.1
Total net sales	\$2,198.7	\$2,156.4	\$2,325.0
Operating income (loss): (Note 1)			
Floor coverings	\$ 186.5	\$ 146.9	\$ 145.0
Building products	122.3	95.1	92.2
Industry products	55.5	40.1	9.3
Ceramic tile (Note 2)	(42.4)	9.9	(168.4)
Unallocated corporate expense	0.1	(36.1)	(34.0)
Total operating income	\$ 322.0	\$ 255.9	\$ 44.1
Depreciation and amortization:			
Floor coverings	\$ 65.5	\$ 53.9	\$ 47.9
Building products	37.5	37.0	36.8
Industry products	17.3	19.1	19.3
Ceramic tile	4.3	4.3	13.5
Corporate	8.1	9.4	5.6
Total depreciation and amortization	\$ 132.7	\$ 123.7	\$ 123.1
Capital additions: (Note 3)			
Floor coverings	\$ 76.6	\$ 117.7	\$ 77.3
Building products	54.4	67.7	49.2
Industry products	16.5	22.5	45.0
Ceramic tile	--	--	9.6
Corporate	8.7	12.8	6.3
Total capital additions	\$ 156.2	\$ 220.7	\$ 187.4
Identifiable assets:			
Floor coverings	\$ 713.8	\$ 687.9	\$ 583.2
Building products	554.9	541.1	513.5
Industry products	248.6	272.8	301.8
Ceramic tile	135.7	168.7	135.8
Corporate	722.5	465.1	615.5
Total assets	\$2,375.5	\$2,135.6	\$2,149.8

Note 1:

Restructuring charges in operating income (millions)	1997	1996	1995
Floor coverings	\$--	\$ 14.5	\$ 25.0
Building products	--	8.3	6.3
Industry products	--	4.0	31.4
Unallocated corporate expense	--	19.7	9.1
Total restructuring charges in operating income	\$--	\$ 46.5	\$ 71.8

Note 2: 1997 operating income includes a \$29.7 million loss as a result of charges incurred by Dal-Tile International Inc. for uncollectible receivables, overstocked inventories and other asset revaluations. 1995 operating income includes a \$177.2 million loss due to the ceramic tile business combination. See "Equity Earnings From Affiliates" on page 40.

Note 3: 1997 and 1995 capital additions for industry segments of property, plant and equipment from acquisitions were \$14.5 million and \$15.6 million, respectively.

The floor coverings segment includes resilient flooring, adhesives, installation and maintenance materials and accessories sold to U.S. commercial and residential segments through wholesalers, retailers and contractors. The Corporate Retail Accounts division provides products and marketing services to home centers, which have become an important part of the company's business. To improve logistical cost-effectiveness, 13 independent regional distribution centers are being established to service these customers (12 of the centers were in place by the end of 1997). To reduce interchannel conflict, segmented resilient flooring products were introduced to allow exclusive product offerings by our customers. Raw materials, especially plasticizers and resins, are a significant cost of resilient flooring products. The company has no influence on the worldwide market of these materials and is subject to cost changes.

The building products segment manufactures both commercial and residential ceiling systems. Grid products, manufactured through the WAVE joint venture with Worthington Industries, have become an important part of this business worldwide. Earnings from this joint venture are included in this segment's operating income and in "Equity Earnings from Affiliates" (see page 40). The major sales activity in this segment is in commercial ceiling systems sold to resale distributors and contractors worldwide, with European sales having a significant impact. Ceiling systems for the residential home segment are sold through wholesalers and retailers, mainly in the United States. Through a joint venture with a Chinese partner, a plant facility in Shanghai manufactures ceilings for the Pacific area.

The industry products segment makes a variety of specialty products for the building, automotive, textile and other industries worldwide. The majority of sales in this segment are flexible pipe insulation used in construction and in original equipment manufacturing. These sales are primarily in Europe, with Germany having the largest concentration due to its regulatory requirements. The major product costs for insulation are raw materials and labor. Strong competition exists in insulation since there are minimal barriers to entry into this market. Gasket materials are sold for new and replacement use in the automotive, construction and farm equipment, appliance, small engine and compressor industries. The automotive and diesel build rates are the most sensitive market drivers for these products. Other products in the industry products segment are textile mill supplies, including cots and aprons sold to equipment manufacturers and textile mills.

The ceramic tile products segment includes ceramic tile sold through home centers, Dal-Tile sales service centers and independent distributors. Ceramic tile products face significant competition from foreign suppliers. Starting in 1996, this segment's results are reported as "Equity Earnings from Affiliates" and are included in operating income.

GEOGRAPHIC AREAS

at December 31 (millions)	1997	1996	1995

Net trade sales:			
United States	\$1,453.1	\$1,419.2	\$1,586.4
Europe	545.6	548.4	558.7
Other foreign	200.0	188.8	179.9

Interarea transfers:			
United States	111.7	105.0	101.1
Europe	14.9	13.2	13.8
Other foreign	29.2	30.4	32.1
Eliminations	(155.8)	(148.6)	(147.0)

Total net sales	\$2,198.7	\$2,156.4	\$2,325.0
=====			
Operating income:			
United States	\$ 236.1	\$ 202.7	\$ 7.7
(see note 2 on page 37)			
Europe	77.2	79.3	62.6
Other foreign	8.6	10.0	7.8
Unallocated corp. income (expense)	0.1	(36.1)	(34.0)

Total operating income	\$ 322.0	\$ 255.9	\$ 44.1
=====			
Identifiable assets:			
United States	\$1,168.9	\$1,180.1	\$1,044.5
Europe	370.4	383.7	406.7
Other foreign	113.8	107.3	83.4
Corporate	722.5	465.1	615.5
Eliminations	(0.1)	(0.6)	(0.3)

Total assets	\$2,375.5	\$2,135.6	\$2,149.8
=====			

United States net trade sales include export sales to non-affiliated customers of \$40.9 million in 1997, \$34.0 million in 1996 and \$32.1 million in 1995. Also included in United States net trade sales were ceramic tile operations sales of \$240.1 million in 1995.

"Europe" includes operations located primarily in England, France, Germany, Italy, the Netherlands, Poland, Spain, Sweden and Switzerland. Operations in Australia, Canada, The People's Republic of China, Hong Kong, Indonesia, Japan, Korea, Singapore and Thailand are in "Other foreign."

Transfers between geographic areas and commissions paid to affiliates marketing exported products are accounted for by methods that approximate arm's-length transactions, after considering the costs incurred by the selling company and the return on assets employed of both the selling unit and the purchasing unit. Operating income of a geographic area includes income accruing from sales to affiliates.

OPERATING STATEMENT ITEMS

NET SALES

Net sales in 1997 totaled \$2,198.7 million, 2.0% above the 1996 total of \$2,156.4 million and 5.4% below the 1995 total of \$2,325.0 million. Prior to 1996, ceramic tile segment sales were consolidated with total company results. Ceramic tile net sales for 1995 were \$240.1 million.

EQUITY (EARNINGS) LOSS FROM AFFILIATES

Equity earnings from affiliates for 1997 were primarily comprised of the company's share of the net loss from the Dal-Tile International Inc. business combination and the amortization of the excess of the company's investment in Dal-Tile over the underlying equity in net assets, and income from the 50% interest in the WAVE joint venture with Worthington Industries. The 1997 loss included \$8.4 million for the company's share of operating losses incurred by Dal-Tile, a \$29.7 million loss for the company's share of the charge incurred by Dal-Tile, primarily for uncollectible receivables and overstocked inventories, and \$4.3 million for the amortization of Armstrong's initial investment in Dal-Tile over the underlying equity in net assets of the business combination. Equity earnings from affiliates for 1996 were primarily comprised of the company's after-tax share of the net income of the Dal-Tile International Inc. business combination and the amortization of the excess of the company's investment in Dal-Tile over the underlying equity in net assets, and the 50% interest in the WAVE joint venture with Worthington Industries. Results in 1995 reflect only the 50% interest in the WAVE joint venture.

In 1995, the company entered into a business combination with Dal-Tile International Inc. The transaction was accounted for at fair value and involved the exchange of \$27.6 million in cash and the stock of the ceramic tile operations, consisting primarily of American Olean Tile Company, a wholly-owned subsidiary, for ownership of 37% of the shares of Dal-Tile. The company's investment in Dal-Tile exceeded the underlying equity in net assets by \$123.9 million which will be amortized over a period of 30 years. The after-tax loss on the transaction was \$116.8 million.

In August 1996, Dal-Tile issued new shares in a public offering decreasing the company's ownership share from 37% to 33%. During 1997, the company purchased additional shares of Dal-Tile stock, increasing the company's ownership to 34%.

Armstrong's ownership of Dal-Tile is accounted for under the equity method. The summarized historical financial information for ceramic tile operations is presented below.

(millions)	1995
Net sales	\$ 240.1
Operating income/(1)/	8.8
Assets/(2)/	269.8
Liabilities/(2)/	17.3

Note 1: Excludes 1995 loss of \$177.2 million due to ceramic tile business combination.

Note 2: 1995 balances were as of December 29, 1995, immediately prior to the ceramic tile business combination.

EARNINGS FROM CONTINUING BUSINESSES

Earnings from continuing businesses were \$185.0 million in 1997 compared with \$164.8 million in 1996 and \$13.6 million in 1995. Earnings from continuing businesses in 1997 included \$38.6 million in losses from its ceramic tile segment mentioned above. Included in the earnings for 1996 and 1995 were after-tax restructuring charges of \$29.6 million and \$46.5 million, respectively. 1995 earnings included the \$116.8 million after-tax loss for the ceramic tile business combination mentioned above.

DISCONTINUED OPERATIONS

In 1995 the company sold the stock of its furniture subsidiary, Thomasville Furniture Industries, Inc., to INTERCO Incorporated for \$331.2 million in cash. INTERCO also assumed \$8.0 million

of interest-bearing debt. The company recorded a gain of \$83.9 million after tax on the sale. Certain liabilities related to terminated benefit plans of approximately \$11.3 million were retained by the company. Thomasville and its subsidiaries recorded sales of approximately \$550.2 million in 1995.

NET EARNINGS

Net earnings were \$185.0 million for 1997 compared with \$155.9 million and \$123.3 million in 1996 and 1995, respectively.

EARNINGS PER SHARE

The following table provides a reconciliation of the numerators and denominators of the basic and diluted per share calculations for earnings (loss) from continuing businesses.

Millions except for per-share data	Earnings (Loss)	Shares	Per-Share Amount
----- For the year ended 1997 -----			
Basic Earnings per Share			
Earnings from continuing businesses	\$ 185.0	40.6	\$ 4.55
Dilutive options		0.4	
Diluted Earnings per Share			
Earnings available for common	\$ 185.0	41.0	\$ 4.50
=====			
For the year ended 1996 -----			
Earnings from continuing businesses	\$ 164.8		
Less: preferred stock dividends	8.8		
Plus: tax benefit on dividends paid on unallocated preferred shares	2.0		
Basic Earnings per Share			
Earnings available for common	\$ 158.0	39.1	\$ 4.04
=====			
Earnings from continuing businesses	\$ 164.8		
Less: increased contribution to the ESOP assuming conversion of preferred shares to common	3.2		
Less: net reduction in tax benefits assuming conversion of the ESOP preferred shares to common	0.6		
Dilutive options		0.4	
Common shares issuable under the ESOP		2.6	
Diluted Earnings per Share			
Earnings available for common	\$ 161.0	42.1	\$ 3.82
=====			
For the year ended 1995 -----			
Earnings from continuing businesses	\$ 13.6		
Less: preferred stock dividends	18.8		
Plus: tax benefit on dividends paid on unallocated preferred shares	4.5		
Basic Earnings per Share			
Earnings (loss) available for common	\$ (0.7)	37.1	\$ (0.02)
=====			
Earnings from continuing businesses	\$ 13.6		
Less: increased contribution to the ESOP assuming conversion of preferred shares to common	7.3		
Less: net reduction in tax benefits assuming conversion of the ESOP preferred shares to common	1.2		
Dilutive options		0.3	
Common shares issuable under the ESOP		5.4	
Diluted Earnings per Share			
Earnings available for common	\$ 5.1	42.8	\$ (0.02)/1/
=====			

Note 1: Diluted earnings (loss) per share from continuing businesses for 1995

was antidilutive.

In 1996, the employee stock ownership plan (ESOP) and retirement savings plan were merged resulting in the conversion of convertible preferred shares into common stock. Basic earnings per share for "Earnings from continuing businesses" in 1996 and 1995 are determined by dividing the earnings, after deducting preferred dividends (net of tax benefits on unallocated shares), by the average number of common shares outstanding, including the converted ESOP shares from the conversion date forward. Diluted earnings per share for 1996 and 1995 include the shares of common stock outstanding, the dilutive effect of stock options and the adjustments to common shares and earnings required to portray the convertible preferred ESOP shares on an "if converted" basis prior to conversion.

In 1997, the company adopted SFAS No. 128, "Earnings per Share," effective December 15, 1997. As a result, the company's reported earnings per share for 1996 and 1995 were restated. The effect of this accounting change on previously reported earnings per-share data was as follows:

Per-share amounts	1996	1995
Primary earnings (loss) from continuing businesses per share as reported	\$ 3.97	\$ (0.02)
Effect of SFAS No. 128	0.07	--
Basic earnings (loss) from continuing businesses per share as restated	\$ 4.04	\$ (0.02)
Fully diluted earnings (loss) from continuing businesses per share as reported	\$ 3.81	\$ (0.02)
Effect of SFAS No. 128	0.01	--
Diluted earnings (loss) from continuing businesses per share as restated	\$ 3.82	\$ (0.02)

RESTRUCTURING CHARGES

Restructuring charges amounted to \$46.5 million in 1996 and \$71.8 million in 1995.

The second-quarter 1996 restructuring charge related primarily to the reorganization of corporate and business unit staff positions; realignment and consolidation of the Armstrong and W.W. Henry installation products businesses; restructuring of production processes in the Munster, Germany, ceilings facility; early retirement opportunities for employees in the Fulton, New York, gasket and specialty paper products facility; and write-down of assets. These actions affected approximately 500 employees, about two-thirds of whom were in staff positions. The charges were estimated to be evenly split between cash payments and noncash charges. The majority of the cash outflow was expected to occur within the following 12 months. It was anticipated that ongoing cost reductions and productivity improvements should permit recovery of these charges in less than two years. The 1995 restructuring charges related primarily to the closure of a plant in Braintree, Massachusetts, and for severance of 670 employees in the North American flooring business and the European industry products and building products businesses.

Actual severance payments charged against restructuring reserves were \$17.2 million in 1997 relating to the elimination of 394 positions, of which 247 terminations occurred since the beginning of 1997. As of December 31, 1997, an immaterial amount remained in the reserves for restructuring actions.

DEPRECIATION AND AMORTIZATION

(millions)	1997	1996	1995
Depreciation	\$ 117.4	\$ 108.6	\$ 114.9
Amortization	15.3	15.1	8.2
Total	\$ 132.7	\$ 123.7	\$ 123.1

Depreciation expense increased in 1997 primarily due to higher capital expenditures in 1996.

SELECTED OPERATING EXPENSES

(millions)	1997	1996	1995
Maintenance and repair costs	\$ 107.3	\$ 105.3	\$ 120.2
Research and development costs	47.8	55.2	57.9
Advertising costs	10.5	18.4	25.5
OTHER EXPENSE (INCOME), NET			
(millions)	1997	1996	1995
Interest and dividend income	\$ (4.9)	\$ (6.5)	\$ (3.3)
Foreign exchange, net loss	0.5	1.2	2.6
Postretirement liability transition obligation	--	--	1.6
Discontinued businesses	0.8	(2.8)	--
Minority interest	0.6	0.3	0.6
Other	0.8	0.9	0.4
Total	\$ (2.2)	\$ (6.9)	\$ 1.9

EMPLOYEE COMPENSATION

Employee compensation and the average number of employees are presented in the table below. Restructuring charges for severance costs and early retirement incentives have been excluded.

Employee compensation cost summary (millions)	1997	1996	1995
Wages and salaries	\$ 494.7	\$ 509.7	\$ 589.2
Payroll taxes	50.7	51.5	61.7
Pension credits	(22.2)	(16.1)	(12.1)
Insurance and other benefit costs	51.9	50.7	58.7
Stock-based compensation	9.6	5.8	0.8
Total	\$ 584.7	\$ 601.6	\$ 698.3
Average number of employees	10,643	10,572	13,433

PENSION COSTS

The company and a number of its subsidiaries have pension plans covering substantially all employees. Benefits from the principal plan are based on the employee's compensation and years of service.

The company also had defined-contribution pension plans for eligible employees at certain of its U.S. subsidiaries, such as the Employee Stock Ownership Plan (ESOP) described on page 47.

Funding requirements, in accordance with provisions of the Internal Revenue Code, are determined independently of expense using an expected long-term rate of return on assets of 8.67%. The company's principal plan was subject to the full funding limitation in 1997, 1996 and 1995, and the company made no contribution to that plan in any of those years.

The total pension cost or credit from all plans is presented in the table below.

Total pension (credit) cost (millions)	1997	1996	1995
U.S. defined-benefit plans:			
Net pension credit	\$ (47.8)	\$ (39.9)	\$ (26.5)
Early retirement incentives	--	10.1	28.7
Net curtailment gain	--	--	(1.2)
Defined contribution plans	10.4	9.9	4.2
Net pension cost of non-U.S. defined-benefit plans	8.2	8.5	8.1
Other funded and unfunded pension costs	7.0	5.4	3.3
Total pension (credit) cost	\$ (22.2)	\$ (6.0)	\$ 16.6

In 1995, the company recognized a \$1.6 million curtailment gain from the sale of the furniture business and a \$0.4 million curtailment loss from the ceramic tile business combination.

The net credit for U.S. defined-benefit pension plans was determined using the assumptions presented in the table below.

Net credit for U.S. defined-benefit pension plans (millions)	1997	1996	1995
Assumptions:			
Discount rate	7.25%	7.00%	8.00%
Rate of increase in future compensation levels	4.50%	4.25%	5.25%
Expected long-term rate of return on assets	8.75%	8.75%	8.75%
Actual return on assets	\$ (324.3)	\$ (124.2)	\$ (406.7)
Less amount deferred	201.5	10.4	313.0
Expected return on assets	\$ (122.8)	\$ (113.8)	\$ (93.7)
Net amortization and other	(11.4)	(9.4)	(9.3)
Service cost--benefits earned during the year	15.8	17.2	16.7
Interest on the projected benefit obligation	70.6	66.1	59.8
Net pension credit	\$ (47.8)	\$ (39.9)	\$ (26.5)

The funded status of the company's U.S. defined-benefit pension plans at the end of 1997 and 1996 is presented in the following table.

Funded status of U.S. defined-benefit pension plans (millions)	1997	1996
Assumptions:		
Discount rate	7.00%	7.25%
Compensation rate	4.00%	4.50%
Actuarial present value of benefit obligations:		
Vested benefit obligation	\$ (911.5)	\$ (824.4)
Accumulated benefit obligation	\$ (977.4)	\$ (899.4)
Projected benefit obligation for services rendered to date	\$(1,048.0)	\$ (981.2)
Plan assets at fair value	\$ 1,754.5	\$ 1,501.9
Plan assets in excess of projected benefit obligation	\$ 706.5	\$ 520.7
Unrecognized transition asset	(27.6)	(33.9)
Unrecognized prior service cost	90.2	99.9
Unrecognized net gain--experience different from assumptions	(604.9)	(462.6)
Provision for restructuring charges	(1.4)	(9.1)
Prepaid pension cost	\$ 162.8	\$ 115.0

The plan assets, stated at estimated fair value as of December 31, are primarily listed stocks and bonds.

The company has pension plans covering employees in a number of foreign countries that utilize assumptions that are consistent with, but not identical to, those of the U.S. plans.

Net cost for non-U.S. defined-benefit

pension plans (millions)	1997	1996	1995
Actual return on assets	\$ (15.4)	\$ (8.4)	\$ (11.2)
Less amount deferred	8.6	2.5	5.9
Expected return on assets	\$ (6.8)	\$ (5.9)	\$ (5.3)
Net amortization and other	0.5	0.5	0.4
Service cost--benefits earned during the year	5.7	5.3	4.9
Interest on the projected benefit obligation	8.8	8.6	8.1
Net pension cost	\$ 8.2	\$ 8.5	\$ 8.1

The funded status of the non-U.S. defined-benefit pension plans at the end of 1997 and 1996 is presented in the following table.

Funded status of non-U.S. defined-benefit pension plans (millions)	1997	1996
Actuarial present value of benefit obligations:		
Vested benefit obligation	\$ (116.4)	\$ (112.8)
Accumulated benefit obligation	\$ (119.3)	\$ (117.2)
Projected benefit obligation for services rendered to date	\$ (127.4)	\$ (125.5)
Plan assets at fair value	95.5	84.5
Projected benefit obligation greater than plan assets	\$ (31.9)	\$ (41.0)
Unrecognized transition obligation	1.4	2.4
Unrecognized prior service cost	5.3	5.1
Unrecognized net gain--experience different from assumptions	(21.8)	(16.9)
Adjustment required to recognize minimum liability	(0.4)	(0.6)
Accrued pension cost	\$ (47.4)	\$ (51.0)

POSTRETIREMENT BENEFITS OTHER THAN PENSIONS AND POSTEMPLOYMENT BENEFITS

The company has postretirement benefit plans that provide for medical and life insurance benefits to certain eligible employees, worldwide, when they retire from active service. The company funds these benefit costs primarily on a pay-as-you-go basis, with the retiree paying a portion of the cost for health care benefits through deductibles and contributions.

The company announced in 1989 and 1990 a 15-year phaseout of its cost of health care benefits for certain future retirees. These future retirees include parent company nonunion employees and some union employees. Shares of ESOP common stock are scheduled to be allocated to these employees, based on employee age and years to expected retirement, to help offset future postretirement medical costs. In addition, they may enroll in a voluntary portion of the ESOP to purchase additional shares.

The postretirement benefit costs were determined using the assumptions presented in the table below.

Periodic postretirement benefit costs (millions)	1997	1996	1995
Assumptions:			
Discount rate	7.25%	7.00%	8.25%
Rate of increase in future compensation levels	4.50%	4.25%	5.25%
Service cost of benefits earned during the year	\$ 3.3	\$ 3.7	\$ 2.8
Interest cost on accumulated postretirement benefit obligation	17.6	17.0	17.1
Net amortization and other	0.3	0.5	(0.8)
Periodic postretirement benefit cost	\$ 21.2	\$ 21.2	\$ 19.1

The status of the company's postretirement benefit plans at the end of 1997 and 1996 is presented in the following table.

Status of postretirement benefit plans (millions)	1997	1996
Assumptions:		
Discount rate	7.00%	7.25%
Compensation rate	4.00%	4.50%
Accumulated postretirement benefit obligation (APBO):		
Retirees	\$ 180.7	\$ 164.9
Fully eligible active plan participants	11.8	14.7
Other active plan participants	70.2	67.5
Total APBO	\$ 262.7	\$ 247.1
Unrecognized prior service credit	6.8	7.8
Unrecognized net loss	(50.9)	(37.9)
Accrued postretirement benefit cost	\$ 218.6	\$ 217.0

The assumed health care cost trend rate used to measure the APBO was 10% in 1996, decreasing 1% per year to an ultimate rate of 6% by the year 2000. The health care cost trend rate assumption has a significant effect on the amounts reported. To illustrate, if the health care cost trend rate assumptions were increased by 1%, the APBO as of December 31, 1997, would be increased by \$22.4 million. The effect of this change on the total of service and interest costs for 1997 would be an increase of \$2.3 million.

The company provides certain postemployment benefits to former or inactive employees and their dependents during the period following employment but before retirement.

Postemployment benefit expense totaled \$3.1 million in 1997, which included a \$3.2 million credit resulting from an increase in the percentage of disabled employees assumed to qualify for Medicare coverage. In 1996, the company recorded postemployment benefit expense of \$3.1 million, which included a \$2.9 million credit resulting from favorable actuarial experience with regard to assumed plan retirement and mortality rates. In 1995, postemployment benefit expense was \$3.2 million, which included a \$4.1 million credit from the transfer of the payment responsibility for certain disability benefits to the company's defined-benefit pension plan.

EMPLOYEE STOCK OWNERSHIP PLAN (ESOP)

In 1989, Armstrong established an Employee Stock Ownership Plan (ESOP) that borrowed \$270 million from banks and insurance companies, repayable over 15 years and guaranteed by the company. The ESOP used the proceeds to purchase 5,654,450 shares of a new series of convertible preferred stock issued by the company. In 1996, the ESOP was merged with the Retirement Savings Plan to form the new Retirement Savings and Stock Ownership Plan (RSSOP). On July 31, 1996, the trustee of the ESOP converted the preferred stock held by the trust into approximately 5.1 million shares of common stock at a one-for-one ratio.

The number of shares released for allocation to participant accounts is based on the proportion of principal and interest paid to the total amount of debt service remaining to be paid over the life of the borrowings. Through December 31, 1997, the ESOP had allocated to participants a total of 1,800,000 shares and retired 800,000 shares.

The ESOP currently covers parent company nonunion employees and some union employees.

The company's guarantee of the ESOP loan has been recorded as a long-term obligation and as a reduction of shareholders' equity on its consolidated balance sheet.

Details of ESOP debt service payments (millions)	1997	1996	1995
Preferred dividends paid	\$ --	\$ 8.9	\$ 18.8
Common stock dividends paid	8.5	4.0	--
Employee contributions	9.7	5.3	6.7
Company contributions	14.7	11.0	6.2
Company loans to ESOP	5.5	4.2	--
Debt service payments made by ESOP trustee	\$ 38.4	\$ 33.4	\$ 31.7

The company recorded costs for the ESOP, utilizing the 80% of the shares allocated method, of \$10.4 million in 1997, \$9.4 million in 1996 and \$3.5 million in 1995. These costs were partially offset by savings realized from changes to company-sponsored health care benefits and elimination of the contribution-matching feature in the company-sponsored voluntary retirement savings plan.

The trustee borrowed \$5.5 million from the company in 1997 and \$4.2 million in 1996. These loans were made to ensure that the financial arrangements provided to employees remain consistent with the original intent of the ESOP.

TAXES

Taxes totaled \$178.5 million in 1997, \$141.6 million in 1996 and \$71.9 million in 1995.

Details of taxes (millions) 1997 1996 1995

Earnings (loss) from continuing businesses before income taxes:

Domestic	\$ 236.4	\$ 176.5	\$ (28.7)
Foreign	92.9	87.6	68.0
Eliminations	(33.1)	(23.9)	(31.1)
Total	\$ 296.2	\$ 240.2	\$ 8.2
Income tax provision (benefit):			
Current:			
Federal	\$ 46.8	\$ 36.2	\$ (19.7)
Foreign	35.7	33.4	23.4
State	1.5	1.4	(0.2)
Total current	84.0	71.0	3.5
Deferred:			
Federal	30.9	4.9	(6.2)
Foreign	(3.7)	(0.5)	(2.7)
Total deferred	27.2	4.4	(8.9)
Total income taxes	111.2	75.4	(5.4)
Payroll taxes	50.7	51.5	61.7
Property, franchise and capital stock taxes	16.6	14.7	15.6
Total taxes	\$ 178.5	\$ 141.6	\$ 71.9

At December 31, 1997, unremitted earnings of subsidiaries outside the United States were \$117.9 million (at December 31, 1997, balance sheet exchange rates) on which no U.S. taxes have been provided. If such earnings were to be remitted without offsetting tax credits in the United States, withholding taxes would be \$5.4 million. The company's intention, however, is to reinvest those earnings permanently or to repatriate them only when it is tax effective to do so.

Reconciliation to U.S. statutory tax rate (millions)	1997	1996	1995
Tax expense at statutory rate	\$ 103.7	\$ 84.1	\$ 2.9
State income taxes	1.0	0.9	--
(Benefit) on ESOP dividend	(0.9)	(1.5)	(2.1)
Tax (benefit) on foreign and foreign-source income	1.1	6.2	(7.7)
Utilization of excess foreign tax credit	(2.9)	(6.5)	--
Equity in (earnings) loss of affiliates	9.9	(4.2)	--
Insurance programs	(0.8)	(1.2)	--
Other items	0.1	(2.4)	(0.1)
Loss from ceramic tile business combination	--	--	1.6
Tax (benefit) expense at effective rate	\$ 111.2	\$ 75.4	\$ (5.4)

EXTRAORDINARY LOSS

In 1996, Dal-Tile refinanced all of its existing debt resulting in an extraordinary loss. The company's share of the extraordinary loss was \$8.9 million after tax, or \$0.21 per diluted share.

BALANCE SHEET ITEMS

CASH AND CASH EQUIVALENTS

Cash and cash equivalents decreased to \$57.9 million at the end of 1997 from \$65.4 million in 1996. Operating and other factors causing the decrease in cash and cash equivalents are detailed in the Consolidated Statements of Cash Flows on page 33.

RECEIVABLES

Accounts and notes receivable (millions)	1997	1996
Customers' receivables	\$ 255.2	\$ 214.7
Customers' notes	15.1	18.4
Miscellaneous receivables	19.8	18.5
	290.1	251.6
Less allowance for discounts and losses	37.5	34.9
Net	\$ 252.6	\$ 216.7

The increase in receivables of \$35.9 million was primarily due to the Swedish flooring and ceiling acquisitions, a higher level of billings related to Corporate Retail Accounts and Building Products and some extended terms in Floor Coverings.

Generally, the company sells its products to select, preapproved groups of customers, whose businesses are directly affected by changes in economic and market conditions. The company considers these factors and the financial condition of each customer when establishing its allowance for losses from doubtful accounts.

Trade receivables are recorded in gross billed amounts as of date of shipment. Provision is made for estimated applicable discounts and losses.

INVENTORIES

Inventories were \$220.1 million in 1997, \$14.4 million higher than 1996. The increase was primarily due to the addition of inventories from the Swedish flooring and ceilings joint ventures.

Approximately 57% of the company's total inventory in 1997 and 1996 was valued on a LIFO (last-in, first-out) basis. Inventory values were lower than would have been reported on a total FIFO (first-in, first-out) basis, by \$60.3 million at the end of 1997 and \$60.6 million at year-end 1996.

Inventories (millions)	1997	1996
------------------------	------	------

Finished goods	\$ 149.4	\$ 143.7
Goods in process	19.9	20.1
Raw materials and supplies	50.8	41.9
Total	\$ 220.1	\$ 205.7

INCOME TAX BENEFITS

Income tax benefits were \$25.9 million in 1997 and \$49.4 million in 1996. Of these amounts, deferred tax benefits were \$21.5 million in 1997 and \$26.9 million in 1996.

OTHER CURRENT ASSETS

Other current assets were \$43.5 million in 1997, an increase of \$16.2 million from the \$27.3 million in 1996, primarily due to an increase in prepaid expenses.

PROPERTY, PLANT AND EQUIPMENT

(millions)	1997	1996
Land	\$ 20.4	\$ 24.4
Buildings	395.4	409.2
Machinery and equipment	1,450.5	1,344.8
Construction in progress	110.2	160.5
	1,976.5	1,938.9
Less accumulated depreciation and amortization	1,004.3	974.9
Net	\$ 972.2	\$ 964.0

The \$37.6 million increase in gross book value to \$1,976.5 million at the end of 1997 included \$141.7 million for capital additions and a \$55.2 million reduction from sales, retirements, dispositions and other changes. Also because of translating property, plant and equipment in foreign currency into U.S. dollars at lower exchange rates, 1997 gross book value was lower by \$48.9 million and net book value declined by \$14.1 million.

The unexpended cost of approved capital appropriations amounted to \$121.2 million at year-end 1997, substantially all of which is scheduled to be expended during 1998.

INSURANCE FOR ASBESTOS-RELATED LIABILITIES

Insurance for asbestos-related liabilities was \$291.6 million reflecting the company's belief in the ultimate availability of insurance in an amount to cover the estimated potential liability of a like amount (see page 55). Such insurance has either been agreed upon or is probable of recovery through negotiation, alternative dispute resolution or litigation. See discussion on pages 59-64.

INVESTMENTS IN AFFILIATES

Investments in affiliates were \$174.9 million in 1997, a decrease of \$29.4 million, reflecting the decrease from the company's 34% share of the Dal-Tile losses somewhat offset by the increase from the 50% interest in the WAVE joint venture.

In 1997 the company purchased additional shares of Dal-Tile for \$9.7 million through open market trades.

OTHER NONCURRENT ASSETS

(millions)	1997	1996
Goodwill and other intangibles	\$ 60.3	\$ 46.1
Pension-related assets	219.8	158.3
Other	56.7	56.8
Total	\$ 336.8	\$ 261.2

Other noncurrent assets increased \$75.6 million in 1997. Goodwill and other intangibles increased \$14.2 million, reflecting higher spending levels in computer software systems and acquired intangibles from acquisitions. The \$61.5 million increase in pension-related assets reflects the net pension credit of \$47.8 million and an increase in the assets of the deferred compensation plans.

ACCOUNTS PAYABLE AND ACCRUED EXPENSES

(millions)	1997	1996
Payables, trade and other	\$ 174.0	\$ 158.2
Asbestos-related claims	72.0	--
Employment costs	47.7	49.7
Restructuring costs	12.2	27.6
Other	34.0	37.8
Total	\$ 339.9	\$ 273.3

INCOME TAXES

(millions)	1997	1996
Payable--current	\$ 32.2	\$ 19.3
Deferred--current	0.8	0.2
Total	\$ 33.0	\$ 19.5

The tax effects of principal temporary differences between the carrying amounts of assets and liabilities and their tax bases are summarized in the following table. Management believes it is more likely than not that the results of future operations will generate sufficient taxable income to realize deferred tax assets.

Deferred income taxes (millions)	1997	1996
Postretirement and postemployment benefits	\$ (87.0)	\$ (87.0)
Restructuring benefits	(7.4)	(13.6)
Asbestos-related liabilities	(82.1)	(49.4)
Capital loss carryforward	(20.4)	(22.1)
Other	(75.0)	(65.8)
Valuation allowance	29.3	22.1
Net deferred assets	\$ (242.6)	\$ (215.8)
Accumulated depreciation	\$ 102.4	\$ 95.6
Pension costs	48.3	38.2
Insurance for asbestos-related liabilities	94.4	49.4
Other	30.5	36.4
Total deferred income tax liabilities	\$ 275.6	\$ 219.6
Net deferred income tax liabilities (assets)	\$ 33.0	\$ 3.8
Less net income tax (benefits)--current	(20.7)	(26.7)
Deferred income taxes--long term	\$ 53.7	\$ 30.5

DEBT

(millions)	1997	Average year-end interest rate	1996	Average year-end interest rate
Short-term debt:				
Commercial paper	\$ 60.8	6.33%	\$ --	--
Foreign banks	23.3	6.23%	14.5	6.81%
Total short-term debt	\$ 84.1	6.30%	\$ 14.5	6.81%
Long-term debt:				
9 3/4% debentures due 2008	\$125.0	9.75%	\$125.0	9.75%
Medium-term notes 8.75-9% due 1998-2001	39.1	8.94%	52.8	8.93%
Bank loans due 1999-2000	25.0	4.74%	21.0	4.79%
Industrial development bonds	19.5	5.10%	19.5	5.25%
Other	29.0	7.76%	14.8	8.57%
Total long-term debt	\$237.6	8.46%	\$233.1	8.67%
Less current installments	14.5	8.91%	13.7	8.91%
Net long-term debt	\$223.1	8.43%	\$219.4	8.65%

Scheduled amortization of long-term debt (millions)

1999	\$25.0	2002	\$--
2000	27.1	2003	--
2001	9.5		

The 9 3/4% debentures and the medium-term notes are not redeemable until maturity and have no sinking-fund requirements.

The bank loans have favorable interest rates.

The industrial development bonds mature in 2004 and 2024 and have favorable interest rates.

Other debt includes an \$18.6 million zero-coupon note due in 2013 that had a carrying value of \$2.5 million at December 31, 1997.

Armstrong has a revolving line of credit of \$300.0 million, expiring in 2001, for general corporate purposes. At December 31, 1997, there were no borrowings under this facility. In addition, the company's foreign subsidiaries have approximately \$109.6 million of unused short-term lines of credit available from banks. Some credit lines are subject to an annual commitment fee.

The company can borrow from its banks generally at rates approximating the lowest available to commercial borrowers and can issue short-term commercial paper notes supported by the lines of credit.

FINANCIAL INSTRUMENTS

The company does not hold or issue financial instruments for trading purposes. The estimated fair value of the company's financial instruments are as follows:

(In millions at December 31)	1997 Carrying amount	Fair value	1996 Carrying amount	Fair value

Assets:				
Cash and cash equivalents	\$ 57.9	\$ 57.9	\$ 65.4	\$ 65.4
Receivables	252.6	252.6	216.7	216.7
Liabilities:				
Short-term and long-term debt	\$321.7	\$356.6	\$247.6	\$281.4
Other noncurrent financial liabilities	172.1	160.1	151.9	141.4
Off-balance sheet financial instruments:				
Foreign currency contract obligations	\$ --	\$ 0.3	\$ --	\$ 1.2
Letters of credit/financial guarantees	--	186.1	--	178.1
Line of credit	--	409.6	--	441.3

Fair values were determined as follows:

The carrying amounts of cash and cash equivalents, receivables, accounts payable and accrued expenses, short-term debt and current installments of long-term debt approximate fair value because of the short-term maturity of these instruments.

The fair value estimates of long-term debt were based upon quotes from major financial institutions taking into consideration current rates offered to the company for debt of the same remaining maturities.

Other noncurrent financial liabilities consist primarily of deferred payments, for which cost approximates fair value.

Foreign currency contract obligations are estimated by obtaining quotes from brokers.

Letters of credit, financial guarantees and line of credit amounts are based on the estimated cost to settle the obligations.

FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISKS

The company does not normally provide collateral or other security to support letters of credit, financial guarantees or lines of credit.

The company is party to forward starting interest rate swaps entered into in anticipation of future debt issuance. The current notional amount under these forward starting swaps is \$100.0 million with all swap initiation dates occurring during 1998. The market value of these forward agreements on December 31, 1997, was \$3.2 million less than the notional amount.

The company uses foreign currency forward contracts and options to reduce the risk that future cash flows from transactions in foreign currencies will be negatively impacted by changes in exchange rates.

The table below provides anticipated net foreign cash flows for goods, services and financing transactions for the next 12 months.

Foreign currency exposure (\$ millions)	Commercial exposure	Financing exposure	Net hedge	Net position
British pound	\$(24.0)	\$(17.1)	\$12.1	\$(29.0)
Canadian dollar	37.0	--	--	37.0
French franc	(17.0)	3.3	(3.3)	(17.0)
German mark	(48.0)	12.4	(12.4)	(48.0)
Italian lira	25.0	2.3	(2.3)	25.0
Spanish peseta	7.0	2.3	(2.3)	7.0

Note 1: A positive amount indicates the company is a net receiver of this currency, while a negative amount indicates the company is a net payer.

The company policy allows hedges of cash flow exposures of up to one year. The table below summarizes the company's foreign currency forward contracts and average contract rates at December 31, 1997. Foreign currency amounts are translated at exchange rates as of December 31, 1997.

Foreign currency contracts (\$ millions)	Forward Contracts			
	Sold	Avg. rate	Bought	Avg. rate
British pound	\$ 5.0	1.68	\$17.1	1.61
Dutch guilder	2.0	2.00	--	--
French franc	3.3	5.9	--	--
German mark	12.4	1.79	--	--
Italian lira	2.3	1726	--	--
Spanish peseta	2.3	151.5	--	--

The foreign currency hedges are straightforward contracts that have no embedded options or other terms that involve a higher level of complexity or risk.

OTHER LONG-TERM LIABILITIES

Other long-term liabilities were \$172.1 million in 1997, an increase of \$20.2 million from \$151.9 million in 1996. Increases of \$4.9 million for pension-related liabilities and \$5.8 million for deferred compensation were the primary causes for the increase. Also included in other long-term liabilities were amounts for workers' compensation, vacation accrual, a reserve for estimated environmental-remediation liabilities (see "Environmental Matters" on the next page) and a \$4.6 million residual reserve for the estimated potential liability primarily associated with claims pending in the company's asbestos-related litigation.

Based upon the company's experience with the asbestos-related litigation--as well as the Wellington Agreement, other settlement agreements with certain of the company's insurance carriers and an earlier interim agreement with several primary carriers--the residual reserve of \$4.6 million is intended to cover potential liability and settlement costs that are not covered by insurance, legal and administrative costs not covered under the agreements and certain other factors that have been involved in the litigation about which uncertainties exist. Future costs of litigation against the company's insurance carriers and other legal costs indirectly related to the litigation, expected to be modest, will be expensed outside the reserve. Amounts, primarily insurance litigation costs, estimated to be payable within one year are included under current liabilities.

This reserve does not address any unanticipated reduction in expected insurance coverage that might result in the future related to pending lawsuits and claims nor any potential shortfall in such coverage for claims that are subject to the settlement class action referred to on pages 59-64.

ASBESTOS-RELATED LIABILITIES

The company reserved \$179.7 million in long-term liabilities and \$72.0 million in current accrued liabilities for asbestos-related claims. The company has recorded an insurance asset (see page 50) in the amount of \$291.6 million for coverage of asbestos-related claims. See discussion on pages 59-64.

ENVIRONMENTAL MATTERS

In 1997, the company incurred capital expenditures of approximately \$1.2 million for environmental compliance and control facilities and anticipates comparable annual expenditures for those purposes for the years 1998 and 1999. The company does not anticipate that it will incur significant capital expenditures in order to meet the requirements of the Clean Air Act of 1990 and the final implementing regulations promulgated by various state agencies.

As with many industrial companies, Armstrong is currently involved in proceedings under the Comprehensive Environmental Response, Compensation and Liability Act ("Superfund"), and similar state laws at approximately 17 sites. In most cases, Armstrong is one of many potentially responsible parties ("PRPs") who have voluntarily agreed to jointly fund the required investigation and remediation of each site. With regard to some sites, however, Armstrong disputes

the liability, the proposed remedy or the proposed cost allocation. Armstrong may also have rights of contribution or reimbursement from other parties or coverage under applicable insurance policies. The company is also remediating environmental contamination resulting from past industrial activity at certain of its current plant sites.

Estimates of future liability are based on an evaluation of currently available facts regarding each individual site and consider factors including existing technology, presently enacted laws and regulations and prior company experience in remediation of contaminated sites. Although current law imposes joint and several liability on all parties at any Superfund site, Armstrong's contribution to the remediation of these sites is expected to be limited by the number of other companies also identified as potentially liable for site costs. As a result, the company's estimated liability reflects only the company's expected share. In determining the probability of contribution, the company considers the solvency of the parties, whether responsibility, is being disputed, the terms of any existing agreements and experience regarding similar matters. The estimated liabilities do not take into account any claims for recoveries from insurance or third parties.

Reserves at December 31, 1997, were for potential environmental liabilities that the company considers probable and for which a reasonable estimate of the potential liability could be made. Where existing data is sufficient to estimate the amount of the liability, that estimate has been used; where only a range of probable liability is available and no amount within that range is more likely than any other, the lower end of the range has been used. As a result, the company has accrued, before agreed-to insurance coverage, \$9.3 million to reflect its estimated undiscounted liability for environmental remediation. As assessments and remediation activities progress at each individual site, these liabilities are reviewed to reflect additional information as it becomes available.

Actual costs to be incurred at identified sites in the future may vary from the estimates, given the inherent uncertainties in evaluating environmental liabilities. Subject to the imprecision in estimating environmental remediation costs, the company believes that any sum it may have to pay in connection with environmental matters in excess of the amounts noted above would not have a material adverse effect on its financial condition, liquidity or results of operations, although the recording of future costs may be material to earnings in such future period.

STOCK-BASED COMPENSATION PLANS

Awards under the 1993 Long-Term Stock Incentive Plan may be in the form of stock options, stock appreciation rights in conjunction with stock options, performance restricted shares and restricted stock awards. No more than 4,300,000 shares of common stock may be issued under the Plan, and no more than 430,000 shares of common stock may be awarded in the form of restricted stock awards. The Plan extends to April 25, 2003. Pre-1993 grants made under predecessor plans will be governed under the provisions of those plans.

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

Changes in option shares outstanding (thousands except for share price)	1997	1996	1995
Option shares at beginning of year	2,161.4	1,841.6	1,612.1
Options granted	286.8	728.7	642.8
Option shares exercised	(265.5)	(376.7)	(390.9)
Stock appreciation rights exercised	(4.7)	(10.8)	(11.5)
Options cancelled	(16.7)	(21.4)	(10.9)
Option shares at end of year	2,161.3	2,161.4	1,841.6
Option shares exercisable at end of year	1,262.1	1,185.8	1,196.7
Shares available for grant	1,585.5	1,914.6	2,838.9
Weighted average price per share:			
Options outstanding	\$ 54.01	\$ 50.06	\$ 43.00
Options exercisable	46.88	41.11	37.93
Options granted	69.63	60.30	52.47
Option shares exercised	39.10	36.27	33.48

The following table summarizes information about stock options outstanding at December 31, 1997.

Stock options outstanding as of 12/31/97					
Range of exercise prices	Options outstanding			Options exercisable	
	Number outstanding at 12/31/97	Weighted- average remaining option life	Weighted- average exercise price	Number exercisable at 12/31/97	Weighted- average exercise price
\$28-38	359,876	4.3	\$31.75	359,876	\$31.75
38-54	361,127	6.4	45.10	361,127	45.10
54-62	846,219	7.7	58.57	527,999	57.91
62-66	306,000	8.1	63.26	10,000	65.50
66-74	288,050	9.2	69.75	3,100	71.15
	2,161,272			1,262,102	

Performance restricted shares issuable under the 1993 Long-Term Stock Incentive Plan entitle certain key executive employees to earn shares of Armstrong's common stock, only if the total company or individual business units meet certain predetermined performance measures during defined performance periods (generally three years). Total company performance measures include Armstrong's total shareholder return relative to a peer group of 12 companies. At the end of the performance periods, common stock awarded will carry additional restriction periods (generally three or four years), whereby the shares will be held in custody by the company until the expiration or termination of the restrictions. Compensation expense will be charged to earnings over the period in which the restrictions lapse. Within the performance periods at the end of 1997 were 109,837 performance restricted shares outstanding, with 6,253 accumulated dividend equivalent shares. Restricted common stock awards will be issued in 1998 based on the performance period ending December 31, 1997. Within the restriction periods at the end of 1997 were 180,199 shares of restricted common stock outstanding, with 9,118 accumulated dividend equivalent shares, based on performance periods ending prior to 1997.

Restricted stock awards can be used for the purposes of recruitment, special recognition and retention of key employees. Awards for 27,700 shares of restricted stock were granted (excluding performance based awards discussed above) during 1997. At the end of 1997, there were 151,039 restricted shares of common stock outstanding with 7,097 accumulated dividend equivalent shares.

On January 1, 1996, the company adopted SFAS No. 123, "Accounting for Stock-Based Compensation," which permits entities to continue to apply the provisions of APB Opinion No. 25 and provide pro forma net earnings and pro forma earnings per share disclosures. Had compensation cost for these plans been determined consistent with SFAS No. 123, the company's net earnings and earnings per share (EPS) would have been reduced to the following pro forma amounts.

(millions)	1997	1996	1995
Net earnings: As reported	\$ 185.0	\$ 155.9	\$ 123.3
Pro forma	180.7	150.7	121.4
Basic EPS: As reported	4.55	3.81	2.94
Pro forma	4.45	3.68	2.89
Diluted EPS: As reported	4.50	3.61	2.68
Pro forma	4.39	3.49	2.64

The fair value of grants was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions for 1997, 1996 and 1995.

	1997	1996	1995
Risk-free interest rates	6.21%	6.17%	6.38%
Dividend yield	2.46%	2.32%	2.39%
Expected lives	5 years	5 years	5 years
Volatility	19%	21%	25%

Because the SFAS No. 123 method of accounting has not been applied to grants prior to January 1, 1995, the resulting pro forma compensation cost may not be representative of that to be expected in future years.

TREASURY SHARES

Treasury share changes for 1997, 1996 and 1995 are as follows:

Years ended December 31 (thousands)	1997	1996	1995
Common shares			
Balance at beginning of year	10,714.6	15,014.1	14,602.1
Stock purchases/(1)/	1,299.2	1,357.6	795.7
Stock issuance activity, net/(2)/	(254.3)	(5,657.1)	(383.7)
Balance at end of year	11,759.5	10,714.6	15,014.1

Note 1: Includes small unsolicited buybacks of shares, shares received under share tax withholding transactions and open market purchases of stock through brokers.

Note 2: 1996 includes 5,057,400 shares issued as a result of conversion of preferred to common stock.

In July 1996, the Board of Directors authorized the company to repurchase an additional 3.0 million shares of its common stock through the open market or through privately negotiated transactions bringing the total authorized common share repurchases to 5.5 million shares. Under the total plan, Armstrong has repurchased approximately 3,661,000 shares through December 31, 1997, with a total cash outlay of \$218.7 million, including 1,281,000 repurchased in 1997.

PREFERRED STOCK PURCHASE RIGHTS PLAN

In 1996, the Board of Directors renewed the company's 1986 shareholder rights plan and in connection therewith declared a distribution of one right for each share of the company's common stock outstanding on and after January 19, 1996. In general, the rights become exercisable at \$300 per right for a fractional share of a new series of Class A preferred stock 10 days after a person or group, other than certain affiliates of the company, either acquires beneficial ownership of shares representing 20% or more of the voting power of the company or announces a tender or exchange offer that could result in such person or group beneficially owning shares representing 28% or more of the voting power of the company. If thereafter any person or group becomes the beneficial owner of 28% or more of the voting power of the company or if the company is the surviving company in a merger with a person or group that owns 20% or more of the voting power of the company, then each owner of a right (other than such 20% shareholder) would be entitled to purchase shares of company common stock having a value equal to twice the exercise price of the right. Should the company be acquired in a merger or other business combination, or sell 50% or more of its assets or earnings power, each right would entitle the holder to purchase, at the exercise price, common shares of the acquirer having a value of twice the exercise price of the right. The exercise price was determined on the basis of the Board's view of the long-term value of the company's common stock. The rights have no voting power nor do they entitle a holder to receive dividends. At the company's option, the rights are redeemable prior to becoming exercisable at five cents per right. The rights expire on March 21, 2006.

LITIGATION AND RELATED MATTERS

ASBESTOS-RELATED LITIGATION

PERSONAL INJURY LITIGATION

The company is one of many defendants in approximately 83,000 pending claims as of December 31, 1997, alleging personal injury from exposure to asbestos. The increase in the number of claims during the last two quarters of 1997 is primarily due to the inclusion of cases that had been subject to an injunction related to the Georgine Settlement Class Action ("Georgine"), described below, and those that had been filed in the tort system against other defendants (and not against the Center for Claims Resolution ("Center") members) while Georgine was pending.

Nearly all claims seek general and punitive damages arising from alleged exposures, at various times, from World War II onward, to asbestos-containing products. Claims against the company generally involve allegations of negligence, strict liability, breach of warranty and conspiracy with respect to its

involvement with asbestos-containing insulation products. The company discontinued the sale of all such products in 1969. The claims also allege that injury may be determined many years (up to 40 years) after first exposure to asbestos. Nearly all suits name many defendants, and over 100 different companies are reportedly involved. The company believes that many current plaintiffs are unimpaired. A large number of claims have been settled, dismissed, put on inactive lists or otherwise resolved, and the company generally is involved in all stages of claims resolution and litigation, including individual trials, consolidated trials and appeals. Neither the rate of future filings and resolutions nor the total number of future claims can be predicted at this time with a high degree of certainty.

Attention has been given by various parties to securing a comprehensive resolution of the litigation. In 1991, the Judicial Panel for Multidistrict Litigation ordered the transfer of federal cases to the Eastern District of Pennsylvania in Philadelphia for pretrial purposes. The company supported this transfer. Some cases are periodically released for trial, although the issue of punitive damages is retained by the transferee court. That court has been instrumental in having the parties resolve large numbers of cases in various jurisdictions and has been receptive to different approaches to the resolution of claims. Claims in state courts have not been directly affected by the transfer, although most recent cases have been filed in state courts.

Georgine Settlement Class Action

Georgine v. Amchem was a settlement class action filed in the Eastern District of Pennsylvania, on January 15, 1993, that included essentially all future personal injury claims against members of the Center, including the company. It was designed to establish a nonlitigation system for the resolution of such claims, and offered a method for prompt compensation to claimants who were occupationally exposed to asbestos if they met certain exposure and medical criteria. Compensation amounts were derived from historical settlement data and no punitive damages were to be paid. The settlement was designed to, among other things, minimize transactional costs, including attorneys' fees, expedite compensation to claimants with qualifying claims, and relieve the courts of the burden of handling future claims. Based on maximum mathematical projections covering a ten-year period starting in 1994, the company estimated in Georgine a reasonably possible additional liability of \$245 million.

The District Court, after exhaustive discovery and testimony, approved the settlement class action and issued a preliminary injunction that barred class members from pursuing claims against Center members in the tort system. The U.S. Court of Appeals for the Third Circuit reversed that decision, and the reversal was sustained by the U.S. Supreme Court on June 25, 1997, holding that the settlement class did not meet the requirements for class certification under Federal Rule of Civil Procedure 23. The preliminary injunction was vacated on July 21, 1997, resulting in the immediate reinstatement of enjoined cases and a loss of the bar against the filing of claims in the tort system. The company believes that an alternative claims resolution mechanism to Georgine is likely to emerge.

Asbestos-related liability

During the last half of 1997, the company assessed the impact of the recent Supreme Court ruling on its projected asbestos resolution and defense costs. In doing so, the company reviewed, among other things, its historical settlement amounts, the incidence of past claims, the mix of the injuries and occupations of the plaintiffs, the number of cases pending against it, the Georgine projection and its experience. Subject to the uncertainties, limitations and other factors referred to above and based upon its experience, the company has recorded \$251.7 million on the balance sheet as an estimated minimum liability to defend and resolve probable and estimable asbestos-related personal injury claims currently pending and to be filed through 2003. This is management's best estimate of the minimum liability, although potential future costs for claims could range up to an additional \$387 million or an estimated maximum liability of approximately \$639 million. Because of the uncertainties related to asbestos litigation, it is not possible to estimate the number of personal injury claims that may be filed after 2003 or their defense and resolution costs. Therefore, the company's estimated liability does not include costs for personal injury claims that may be filed after 2003, although it is likely there will be such additional claims. Management believes that the potential additional costs for claims to be filed through 2003 and those filed thereafter, net of any potential insurance recoveries, will not have a material after-tax effect on the financial condition of the company or its liquidity, although the net after-tax effect of any future liabilities recorded in excess of insurance assets could be material to earnings in a future period.

PROPERTY DAMAGE LITIGATION

The company is also one of many defendants in 10 pending claims as of December 31, 1997, brought by public and private building owners. These claims include allegations of damage to buildings caused by asbestos-containing products and generally seek compensatory and punitive damages and equitable relief, including reimbursement of expenditures, for removal and replacement of such products. The claims appear to be aimed at friable (easily crumbled) asbestos-containing products, although allegations encompass all asbestos-containing products, including previously installed asbestos-containing resilient flooring. Among the lawsuits that have been resolved are four class actions, which involve public and private schools, Michigan state public and private schools, colleges and universities, and private property owners who leased facilities to the federal government. The company vigorously denies the validity of the allegations against it in these claims. These suits and claims are not handled by the Center. Insurance coverage has been resolved and is expected to cover almost all costs of these claims.

CODEFENDANT BANKRUPTCIES

Certain codefendant companies have filed for reorganization under Chapter 11 of the Federal Bankruptcy Code. As a consequence, litigation against them (with some exceptions) has been stayed or restricted. Due to the uncertainties involved, the long-term effect of these proceedings on the litigation cannot be predicted.

INSURANCE COVERAGE

The company's primary and excess insurance policies provide product hazard and nonproducts (general liability) coverages for personal injury claims, and product hazard coverage for property damage claims. Certain policies also provide coverage to ACandS, Inc., a former subsidiary of the company. The company and ACandS, Inc., share certain limits that both have accessed and have entered into an agreement that reserved for ACandS, Inc., a certain amount of excess insurance.

California Insurance Coverage Lawsuit

Trial court decisions in the insurance lawsuit filed by the company in California held that the trigger of coverage for personal injury claims was continuous from exposure through death or filing of a claim, that a triggered insurance policy should respond with full indemnification up to policy limits, and that any defense obligation ceases upon exhaustion of policy limits. Although not as comprehensive, another decision established favorable defense and indemnity coverage for property damage claims, providing coverage during the period of installation and any subsequent period in which a release of fibers occurred. The California appellate courts substantially upheld the trial court, and that insurance coverage litigation is now concluded. The company has resolved most personal injury products hazard coverage matters with its solvent carriers through the Wellington Agreement, referred to below, or other settlements. In 1989, a settlement with a carrier having both primary and excess coverages provided for certain minimum and maximum percentages of costs for personal injury claims to be allocated to nonproducts (general liability) coverage, the percentage to be determined by negotiation or in alternative dispute resolution ("ADR").

The insurance carriers that provided personal injury products hazard, nonproducts or property damage coverages are as follows: Reliance Insurance Company; Aetna (now Travelers) Casualty and Surety Company; Liberty Mutual Insurance Company; Travelers Insurance Company; Fireman's Fund Insurance Company; Insurance Company of North America; Lloyds of London; various London market companies; Fidelity and Casualty Insurance Company; First State Insurance Company; U.S. Fire Insurance Company; Home Insurance Company; Great American Insurance Company; American Home Assurance Company and National Union Fire Insurance Company (known as the AIG Companies); Central National Insurance Company; Interstate Insurance Company; Puritan Insurance Company; and Commercial Union Insurance Company. Midland Insurance Company, an excess carrier that provided \$25 million of personal injury coverage, certain London companies, and certain excess carriers providing only property damage coverage are insolvent. The company is pursuing claims against insolvents in a number of forums.

Wellington Agreement

In 1985, the company and 52 other companies (asbestos defendants and insurers) signed the Wellington Agreement. This Agreement settled nearly all disputes concerning personal injury insurance coverage with most of the company's carriers, provided broad coverage for both defense and indemnity and addressed both products hazard and non-products (general liability) coverages.

Asbestos Claims Facility ("Facility") and Center for Claims Resolution

The Wellington Agreement established the Facility to evaluate, settle, pay and defend all personal injury claims against member companies. Resolution and defense costs were allocated by formula. The Facility subsequently dissolved, and the Center was created in October 1988 by 21 former Facility members, including the company. Insurance carriers, while not members, are represented ex officio on the Center's governing board and have agreed annually to provide a portion of the Center's operational costs. The Center adopted many of the conceptual features of the Facility and has addressed the claims in a manner consistent with the prompt, fair resolution of meritorious claims. Resolution and defense costs are allocated by formula; adjustments over time have resulted in some increased share for the company.

Insurance Recovery Proceedings

A substantial portion of the company's primary and excess insurance asset is nonproducts (general liability) insurance for personal injury claims, including among others, those that involve exposure during installation of asbestos materials. The Wellington Agreement and the 1989 settlement agreement referred to above have provisions for such coverage. An ADR process under the Wellington Agreement is underway against certain carriers to determine the percentage of resolved and unresolved claims that are nonproducts claims, to establish the entitlement to such coverage and to determine whether and how much reinstatement of prematurely exhausted products hazard insurance is warranted. The nonproducts coverage potentially available is substantial and, for some policies, includes defense costs in addition to limits. The carriers have raised various defenses, including waiver, laches, statutes of limitations and contractual defenses. One primary carrier alleges that it is no longer bound by the Wellington Agreement, and another alleges that the company agreed to limit its claims for nonproducts coverage against that carrier when the Wellington Agreement was signed. The ADR process is in the trial phase of binding arbitration. Other proceedings against non-Wellington carriers may become necessary.

An insurance asset in the amount of \$291.6 million is recorded on the balance sheet and reflects the company's belief in the availability of insurance in this amount, based upon the company's success in insurance recoveries, settlement agreements that provide such coverage, the nonproducts recoveries by other companies and the opinion of outside counsel. Such insurance is probable of recovery through negotiation or litigation. A substantial portion of the insurance asset is in ADR, which the company believes may be resolved in 1998 or later. A shortfall has developed between available insurance and amounts necessary for resolution and defense costs. This shortfall was \$39.9 million at the end of 1997 and included a \$1.5 million insurance recovery from an insolvent insurance carrier. The recovery of insurance assets to cover the shortfall will depend upon the resolution of the ADR and other disputes with the insurance carriers. The company does not believe that after-tax effect of the shortfall will be material either to the financial condition of the company or to its liquidity.

CONCLUSIONS

The company does not know how many claims will be filed against it in the future, or the details thereof or of pending suits not fully reviewed, or the defense and resolution costs that may ultimately result therefrom, or whether an alternative to the Georgine settlement vehicle may emerge, or the scope of its insurance coverage ultimately deemed available.

The company has assessed the impact of the recent Supreme Court ruling on its projected asbestos resolution and defense costs. Subject to the uncertainties, limitations and other factors referred to above and based upon its experience, the company has recorded on the balance sheet \$251.7 million as a minimum estimated liability to defend and resolve probable and estimable asbestos-related personal injury claims currently pending and to be filed through 2003. This is management's best estimate of the minimum liability, although potential future costs for these claims could range up to an additional \$387 million or an estimated maximum liability of approximately \$639 million. Because of the uncertainties related to asbestos litigation, it is not possible to estimate the number of personal injury claims that may be filed after 2003 or their cost. Therefore, the company's estimated liability does not include costs for personal injury claims that may be filed after 2003, although it is likely there will be such additional claims. Management believes that the potential additional costs for claims to be filed through 2003 and those filed thereafter, net of any potential insurance recoveries, will not have a material after-tax effect on the financial condition of the company or its liquidity, although the net after-tax effect of any future liabilities recorded in excess of insurance assets could be material to earnings in a future period.

An insurance asset in the amount of \$291.6 million is recorded on the balance sheet and reflects the company's belief in the availability of insurance in this amount, based upon the company's success in insurance recoveries, settlement agreements that provide such coverage, the nonproducts recoveries by other companies, and the opinion of outside counsel. Such insurance is probable of recovery through negotiation or litigation. A substantial portion of the insurance asset is in ADR, which the company believes may be resolved in 1998 or later. A shortfall has developed between available insurance and amounts necessary for resolution and defense costs. This shortfall was \$39.9 million at the end of 1997 and included a \$1.5 million insurance recovery from an insolvent insurance carrier. The recovery of insurance assets to cover the shortfall will depend upon the resolution of the ADR and other disputes with the insurance carriers. The company does not believe that after-tax effect of the shortfall will be material either to the financial condition of the company or to its liquidity.

The company believes that a claims resolution mechanism alternative to the Georgine settlement will eventually emerge, and that the resolution and defense costs are likely to be higher than the earlier maximum mathematical projection in Georgine.

Subject to the uncertainties, limitations and other factors referred to elsewhere in this note and based upon its experience, the company believes it is probable that substantially all of the defense and resolution costs of property damage claims will be covered by insurance.

Even though uncertainties remain as to the potential number of unasserted claims and the liability resulting therefrom, and after consideration of the factors involved, including the ultimate scope of its insurance coverage, the Wellington Agreement and other settlements with insurance carriers, the results of the California insurance coverage litigation, the establishment of the Center, the likelihood that an alternative to the Georgine settlement will eventually emerge, and its experience, the company believes the asbestos-related claims against the company would not be material either to the financial condition of the company or to its liquidity, although the net after-tax effect of any future liabilities recorded in excess of insurance assets could be material to earnings in such future period.

Independent auditors' report

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

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

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Armstrong World Industries, Inc. and subsidiaries as of December 31, 1997 and 1996, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1997, in conformity with generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

KPMG PEAT MARWICK LLP

Philadelphia, PA
February 13, 1998

Item 9. Changes in and Disagreements with Accountants on Accounting and

Financial Disclosure

Not applicable.

PART III

Item 10. Directors and Executive Officers of the Registrant

Directors of the Registrant

The information appearing in the tabulation in the section captioned "Election of Directors" on pages 1-5 of the Company's 1998 Proxy Statement is incorporated by reference herein.

Executive Officers of the Registrant

George A. Lorch* -- Age 56; Chairman of the Board since April 25, 1994; and President (Chief Executive Officer) since September 7, 1993; Executive Vice President 1988-1993.

Marc R. Olivie -- Age 44; President, Worldwide Building Products Operations since October 15, 1996; and the following positions with Sara Lee Corporation

(branded consumer products): President, Sara Lee Champion Europe, Inc. (Italy)

March 1994-October 1996; Vice President, Corporate Development, Sara Lee/DE (Netherlands) September 1993-March 1994; Executive Director, Corporate Development, Sara Lee Corporation (Chicago, Illinois/France) April 1990-September 1993.

Robert J. Shannon, Jr. -- Age 49, President, Worldwide Floor Products Operations since February 1, 1997; President Floor Products Operations International February 1, 1996, through February 1, 1997; President American Olean Tile Company, Inc. March 1, 1992 through December 29, 1995.

Stephen E. Stockwell -- Age 52; President, Corporate Retail Accounts Division since November 22, 1994; Vice President, Corporate Retail Accounts July 1, 1994, through November 22, 1994; General Manager, Residential Sales, Floor Division January 26, 1994 through July 1, 1994; Field Sales Manager, Floor Division, 1988-1994.

Ulrich J. Weimer -- Age 53; President, Armstrong Insulation Products since February 1, 1996; Geschäftsführer, Armstrong World Industries G.m.b.H. since December 11, 1995; General Manager, Worldwide Insulation Products Operations February 1, 1993 through June 1, 1995.

Douglas L. Boles -- Age 40; Senior Vice President, Human Resources since March 1, 1996; and the following positions with PepsiCo (consumer products):

Vice President of Human Resources, Pepsi Foods International Europe Group (U.K.) June 1995-February 1996; Vice President of Human Resources, Walkers Snack Foods (U.K.) March 1994-June 1995; Vice President of Human Resources, Snack Ventures Europe (Netherlands) September 1992-March 1994.

Deborah K. Owen -- Age 46; Senior Vice President, Secretary and General Counsel since January 1, 1998; Attorney, Law Offices of Deborah K. Owen, Columbia, MD, September 1996-September 1997; Partner, Arent Fox Kintner Poltkin & Kahn law firm, Washington DC, August 1994-August 1996; Commissioner, Federal Trade Commission, Washington, DC, October 1989-August 1994.

Frank A. Riddick, III -- Age 40; Senior Vice President, Finance and Chief Financial Officer since April 1995; and the following positions with FMC Corporation, Chicago, IL (chemicals, machinery): Controller May 1993-March 1995; Treasurer December 1990-May 1993.

Edward R. Case -- Age 51; Vice President and Treasurer since May 8, 1996; and the following positions with Campbell Soup Company (branded food products):

Director, Corporate Development October 1994-May 1996; Director, Financial

Planning, U.S. Soup May 1993-September 1994; Deputy Treasurer September 1991-April 1993.

Bruce A. Leech, Jr. -- Age 55; Controller since February 1, 1990.

All information presented above is current as of March 1, 1998. The term of office for each Executive Officer in his present capacity is one year, and each such Executive Officer will serve until reelected or until a successor is elected at the annual meeting of directors which follows the annual shareholders' meeting. Each Executive Officer has been employed by the Company in excess of five continuous years with the exception of Messrs. Boles, Case, Olivie, Riddick and Ms. Owen.

(*Member of the Executive Committee of the Board of Directors as of March 1, 1998.

Item 11. Executive Compensation

The information appearing in the sections captioned "Directors' Compensation" on pages 5-6 and "Executive Officers' Compensation," (other than the information contained under the subcaption "Performance Graph") and "Retirement Income Plan Benefits," on pages 11-15 of the Company's 1998 Proxy Statement is incorporated by reference herein.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information appearing in the sections captioned "Stock Ownership of Certain Beneficial Owners" on page 17 and "Directors' and Executive Officers' Security Ownership" on page 7 of the Company's 1998 Proxy Statement is incorporated by reference herein.

Item 13. Certain Relationships and Related Transactions

Not applicable.

PART IV

Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

The financial statements and schedules filed as a part of this Annual Report on Form 10-K are listed in the "Index to Financial Statements and Schedules" on page 72.

a. The following exhibits are filed as a part of this Annual Report on Form 10-K:

Exhibits

- No. 3(a) Copy of registrant's By-laws, as amended effective March 9, 1998.
- No. 3(b) Registrant's restated Articles of Incorporation, as amended, are incorporated by reference herein from registrant's 1994 Annual Report on Form 10-K wherein they appear as Exhibit 3(b).
- No. 4(a) Registrant's Rights Agreement effective as of March 21, 1996, between the registrant and Chemical Mellon Shareholder Services, L.L.C., as Rights Agent, relating to the registrant's Preferred Stock Purchase Rights is incorporated by reference herein from registrant's registration statement on Form 8-A/A dated March 15, 1996, wherein it appeared as Exhibit 4.
- No. 4(b) Registrant's Retirement Savings and Stock Ownership Plan as amended and restated effective October 1, 1996, is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K where it appeared as Exhibit 4(b). *
- No. 4(d) Registrant's Indenture, dated as of March 15, 1988, between the registrant and Morgan Guaranty Trust Company of New York, as Trustee, as to which The First National Bank of Chicago is successor trustee, is incorporated herein by reference from registrant's 1995 Annual Report on Form 10-K wherein it appeared as Exhibit 4(c).
- No. 4(e) Registrant's Supplemental Indenture dated as of October 19, 1990, between the registrant and The First National Bank of Chicago, as Trustee, is incorporated by reference herein from registrant's 1994 Annual Report on Form 10-K wherein it appeared as Exhibit 4(d).
- No. 10(i)(a) Copy of Agreement Concerning Asbestos-Related Claims dated June 19, 1985, (the "Wellington Agreement") among the registrant and other companies.
- No. 10(i)(b) Producer Agreement concerning Center for Claims Resolution dated September 23, 1988, among the registrant and other companies as amended is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K wherein it appeared as Exhibit 10(i)(b).
- No. 10(i)(c) Credit Agreement between the registrant, certain banks listed therein, and Morgan Guaranty Trust Company of New York, as Agent, dated as of February 7, 1995, providing for a \$200,000,000 credit facility, is incorporated by reference herein from registrant's 1994 Annual Report on Form 10-K wherein it appeared as Exhibit 10(i)(c).
- No. 10(iii)(a) Registrant's Long-Term Stock Option Plan for Key Employees, as amended, is incorporated by reference herein from registrant's 1995 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(a). *

- No. 10(iii)(b) Registrant's Deferred Compensation Plan for Nonemployee Directors, as amended, is incorporated by reference herein from registrant's 1994 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(b). *
- No. 10(iii)(c) Registrant's Directors' Retirement Income Plan, as amended, is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(c). *
- No. 10(iii)(d) Registrant's Management Achievement Plan for Key Executives, as amended, is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(d). *
- No. 10(iii)(e) Registrant's Retirement Benefit Equity Plan (formerly known as the Excess Benefit Plan), as amended, is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(e). *
- No. 10(iii)(f) Armstrong Deferred Compensation Plan, as amended, is incorporated by reference herein from registrant's 1994 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(f). *
- No. 10(iii)(g) Registrant's Employment Protection Plan for Salaried Employees of Armstrong World Industries, Inc., as amended, is incorporated by reference herein from registrant's 1994 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(g). *
- No. 10(iii)(h) Registrant's Restricted Stock Plan For Nonemployee Directors, as amended, is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(h). *
- No. 10(iii)(i) Registrant's Severance Pay Plan for Salaried Employees, is incorporated by referenced herein from registrant's 1994 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(i). *
- No. 10(iii)(j) Copy of registrant's 1993 Long-Term Stock Incentive Plan as amended. *
- No. 10(iii)(k) Form of Agreement between the Company and certain of its Executive Officers, together with a schedule identifying those executives is incorporated by reference herein from registrant's quarterly report on Form 10-Q for the quarter ended September 30, 1997, wherein it appeared as Exhibit 10. *
- No. 10(iii)(l) Form of Indemnification Agreement between the registrant and each of the registrant's Nonemployee Directors, is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(l). *
- No. 11 A statement regarding computation of per share earnings on both basic and diluted bases is

set forth in the Financial Statement Schedules on pages 73 and 74 of this Annual Report on Form 10-K.

- No. 21 List of the registrant's domestic and foreign subsidiaries.
- No. 23 Consent of Independent Auditors.
- No. 24 Powers of Attorney and authorizing resolutions.
- No. 27.1 Financial Data Schedule
- No. 27.2 Restated Financial Data Schedule
- No. 27.3 Restated Financial Data Schedule

* Compensatory Plan

b. During the last quarter of 1997, no reports on Form 8-K were filed.

This 10-K contains certain "forward looking statements" (within the meaning of the Private Securities Litigation Reform Act of 1995). Among other things, they pertain to the Company's earnings, liquidity and financial condition; the ultimate outcome of the Company's asbestos-related litigation (including the likelihood that an alternative to the Georgine settlement will be negotiated); and certain operational matters. Words or phrases denoting the anticipated results of future events - such as "anticipate," "believe," "estimate," "expect," "will likely," "are expected to," "will continue," "project," and similar expressions that denote uncertainty - are intended to identify such forward-looking statements. Actual results may differ materially from anticipated future results: (1) as a result of risk and uncertainties identified in connection with those forward-looking statements, including those factors identified under the sections captioned "Outlook" in Management's Discussion and Analysis of Financial Condition and Results of Operations and those factors identified under the caption "Litigation and Related Matters" in the Notes to Consolidated Financial Statements in connection with the Company's asbestos-related litigation; (2) as a result of factors over which the company has no control, including the strength of domestic and foreign economies, sales growth, competition and certain costs increases; or (3) if the factors on which the Company's conclusions are based do not conform to the Company's expectations.

SIGNATURES

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

ARMSTRONG WORLD INDUSTRIES, INC.

(Registrant)

By /s/ George A. Lorch

Chairman

Date March 20, 1998

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Directors and Principal Officers of the registrant:

George A. Lorch	Chairman and President (Principal Executive Officer)
Frank A. Riddick, III	Senior Vice President, Finance (Principal Financial Officer)
Bruce A. Leech, Jr.	Controller (Principal Accounting Officer)
H. Jesse Arnelle	Director
Van C. Campbell	Director
Donald C. Clark	Director
James. E. Marley	Director
David W. Raisbeck	Director
J. Phillip Samper	Director
Jerre L. Stead	Director

By /s/ George A. Lorch

(George A. Lorch, as
attorney-in-fact and
on his own behalf)
As of March 20, 1998

ARMSTRONG WORLD INDUSTRIES, INC. AND SUBSIDIARIES

Index to Financial Statements and Schedules

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

Consolidated Balance Sheets as of December 31, 1997 and 1996

Consolidated Statements of Earnings for the Years Ended December 31, 1997, 1996, and 1995

Consolidated Statements of Cash Flows for the Years Ended December 31, 1997, 1996, and 1995

Consolidated Statements of Shareholders' Equity for the Years Ended December 31, 1997, 1996, and 1995

Notes to Consolidated Financial Statements

The following additional financial data should be read in conjunction with the financial statements. Schedules not included with this additional data have been omitted because they are not applicable or the required information is presented in the financial statements or the financial review.

Additional Financial Data -----	Page No. -----
Computation for Basic Earnings per Share	73
Computation for Diluted Earnings per Share	74
Schedule II - Valuation and Qualifying Reserves	75

COMPUTATION FOR BASIC EARNINGS PER SHARE
FOR THE YEARS ENDED DECEMBER 31
(AMOUNTS IN MILLIONS EXCEPT FOR PER-SHARE DATA)

	1997	1996	1995
	----	----	----
Common Stock and Common Stock Equivalents			

Average number of common shares outstanding	40.6	39.1	37.1
	====	====	====
 Basic Earnings Per Share			
Earnings from continuing businesses	\$185.0	\$164.8	\$13.6
Less:			
Dividend requirement on Series A convertible preferred stock	--	8.8	18.8
Plus:			
Tax benefit on dividends paid on unallocated preferred shares	--	2.0	4.5
	----	----	----
 Pro forma earnings (loss) available for common			

shareholders:			

Continuing businesses	185.0	158.0	(0.7)
Discontinued business	--	--	109.7
	-----	-----	-----
Before Extraordinary Loss	185.0	158.0	109.0
Extraordinary Loss	--	(8.9)	--
	-----	-----	-----
Net Earnings	\$185.0	\$149.1	\$109.0
	=====	=====	=====
 Basic earnings (loss) per share of common stock			

Continuing businesses	\$ 4.55	\$ 4.04	\$(0.02)
Discontinued business	--	--	2.96
	-----	-----	-----
Before Extraordinary Loss	4.55	4.04	2.94
Extraordinary Loss	--	(0.23)	--
	-----	-----	-----
Net Earnings	\$ 4.55	\$ 3.81	\$ 2.94
	=====	=====	=====

Exhibit No. 11(b)

**COMPUTATION FOR DILUTED EARNINGS PER SHARE
FOR THE YEARS ENDED DECEMBER 31
(AMOUNTS IN MILLIONS EXCEPT FOR PER-SHARE DATA)**

	1997	1996	1995
	----	----	----
Common Stock and Common Stock Equivalents			

Average number of common shares outstanding	40.6	39.1	37.1
Average number of common shares issuable under stock options	0.4	0.4	0.3
Average number of common shares issuable under the Employee Stock Ownership Plan	--	2.6	5.4
	----	---	---
Average number of common and common equivalent shares outstanding	41.0	42.1	42.8
	====	====	====
Adjustments to Earnings			

Earnings from continuing businesses	\$185.0	\$164.8	\$13.6
Less:			
Increased contribution to the Employee Stock Ownership Plan assuming conversion of preferred shares to common	--	3.2	7.3
Net reduction in tax benefits assuming conversion of the Employee Stock Ownership Plan preferred shares to common	--	0.6	1.2
	----	---	---
Pro forma earnings available for common shareholders:			

Continuing businesses	185.0	161.0	5.1
Discontinued business	--	--	109.7
	----	----	----
Before Extraordinary Loss	185.0	161.0	114.8
Extraordinary Loss	--	(8.9)	--
	----	----	----
Net Earnings	\$185.0	\$152.1	\$114.8
	=====	=====	=====
Diluted earnings (loss) per share of common stock			

Continuing businesses	\$4.50	\$3.82 (a)	\$(0.02)
Discontinued business	--	--	2.56
	----	----	----
Before Extraordinary Loss	\$4.50	\$3.82	\$2.68
Extraordinary Loss	--	(0.21)	--
	----	----	----
Net Earnings	\$4.50	\$3.61	\$2.68
	=====	=====	=====

(a) Diluted earnings (loss) per share from continuing businesses for 1995 was antidilutive.

SCHEDULE II

Valuation and Qualifying Reserves of Accounts Receivable

For Years Ended December 31

(amounts in millions)

Provision for Losses -----	1997 ----	1996 ----	1995 ----
Balance at Beginning of Year	\$10.9	\$ 8.7	\$ 9.7
Additions Charged to Earnings	7.3	5.4	2.9
Deductions	5.4	3.2	3.9
Balance at End of Year	\$12.8	\$10.9	\$ 8.7

Provision for Discounts -----			
Balance at Beginning of Year	\$24.0	\$20.3	\$17.3
Additions Charged to Earnings	76.7	74.5	82.2
Deductions	76.0	70.8	79.2
Balance at End of Year	\$24.7	\$24.0	\$20.3

Provision for Discounts and Losses -----			
Balance at Beginning of Year	\$34.9	\$29.0	\$27.0
Additions Charged to Earnings	84.0	79.9	85.1
Deductions	81.4	74.0	83.1
Balance at End of Year	\$37.5	\$34.9	\$29.0

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No. 10(iii)(1)	Form of Indemnification Agreement between the registrant and each of the registrant's Nonemployee Directors, is incorporated by reference herein from registrant's 1996 Annual Report on Form 10-K wherein it appeared as Exhibit 10(iii)(1). *
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No. 27.3	Restated Financial Data Schedule

* Compensatory Plan

Exhibit 3(a)

Bylaws

of

Armstrong

**ARMSTRONG WORLD INDUSTRIES, INC.
LANCASTER, PENNSYLVANIA
EFFECTIVE MARCH 9, 1998**

ARTICLE I

Office

The principal office of the Company shall be in Lancaster, Pennsylvania.

All meetings of directors and stockholders shall be held at the principal office of the Company unless the Board of Directors shall decide otherwise, in which case such meetings may be held within or without the Commonwealth of Pennsylvania as the Board may from time to time direct.

ARTICLE II

Stockholder's Meetings

An annual meeting of stockholders shall be held in each calendar year on such date and at such time as may be fixed by the Board of Directors for the purpose of electing directors and the transaction of such other business as may properly come before the meeting.

Special meetings of the stockholders may be called at any time by the President or the Board of Directors. At any time, upon written request of any person or persons who have duly called a special meeting, it shall be the duty of the Secretary to fix the date of the meeting, to be held not more than sixty days after the receipt of the request, and to give due notice thereof. If the Secretary shall neglect or refuse to fix the date of the meeting and give notice thereof, the person or persons calling the meeting may do so.

Special meetings of the holders of No Par Preferred Stock for the purpose of electing directors may be called as provided in the Articles of Incorporation, as amended.

Written notice of the place, day, and hour of all meetings of stockholders and, in the case of a special meeting, of the general nature of the business to be transacted, shall be given to each stockholder of record entitled to vote at the particular meeting either personally or by sending a copy of the notice through the mail, or by telegram, charges prepaid, to the address of the stockholder appearing on the books of the Company or supplied by him to the Company for the purpose of notice. Except as otherwise provided by these bylaws or by law, such notice shall be given at least five days before the date of the meeting by the President, Vice President, or Secretary. A waiver in writing of any written notice required to be given, signed by the person entitled to such notice, whether before or after the time stated, shall be deemed equivalent to the giving of such notice. Attendance of a person, either in person or by proxy, at any meeting shall constitute a waiver of notice of such meeting, except where a person attends a meeting for the express purpose of objecting to the transaction of any business because the meeting was not lawfully called or convened.

Nominations of candidates for election to the Board of Directors may be made by the Board of Directors or by any stockholder of the Company entitled to notice of, and to vote at, any meeting called for the election of directors. Nominations, other than those made by or on behalf of the Board of Directors of the Company, shall be made in writing and shall be received by the Secretary of the Company not later than (i), with respect to an election of directors to be held at an annual meeting of stockholders, ninety (90) days prior to the anniversary date of the immediately preceding annual meeting and

(ii), with respect to an election of directors to be held at a special meeting of stockholders, the close of business on the tenth (10th) day following the date on which notice of such meeting is first given to stockholders or public disclosure of the meeting is made, whichever is earlier. Such notification shall contain the following information to the extent known to the notifying stockholder: (a) the name, age, business address, and residence address of each proposed nominee and of the notifying stockholders; (b) the principal occupation of each proposed nominee; (c) a representation that the notifying stockholder intends to appear in person or by proxy at the meeting to nominate the person or persons specified in the notice; (d) the class and total number of shares of the Company that are beneficially owned by the notifying stockholders and, if known, by the proposed nominee; (e) the total number of shares of the Company that will be voted by the notifying stockholder for each proposed nominee; (f) a description of all arrangements or understandings between the notifying stockholders and each nominee and any other person or persons (naming such person or persons) pursuant to which the nomination or nominations are to be made by the notifying stockholder; (g) such other information regarding each nominee proposed by such stockholder as would be required to be included in a proxy statement filed with the Securities and Exchange Commission pursuant to Rule 14(a) under the Securities Exchange Act of 1934, as amended, had the nominee been nominated, or intended to be nominated, by the Board of Directors; and (h) the consent of each nominee to serve as a director of the Company if so elected. Nominees of the Board of Directors shall, to the extent appropriate, provide the same information about themselves as in (a) through (h) above to the Secretary of the Company. The Company may request any proposed nominee to furnish such other information as may reasonably be required by the Company to determine the qualifications of the proposed nominee to serve as a director of the Company. Within fifteen (15) days following the receipt by the Secretary of a stockholder notice of nomination pursuant hereto, the Board Affairs and Governance Committee shall instruct the Secretary of the Company to advise the notifying stockholder of any deficiencies in the notice as determined by the Committee. The notifying stockholder shall cure such deficiencies within fifteen

(15) days of receipt of such notice. No persons shall be eligible for election as a director of the Company unless nominated in accordance herewith. Nominations not made in accordance herewith may, in the discretion of the presiding officer at the meeting and with the advice of the Board Affairs and Governance Committee, be disregarded by the presiding officer and, upon his or her instructions, all votes cast for each such nominee may be disregarded. The determinations of the presiding officer at the meeting shall be conclusive and binding upon all stockholders of the Company for all purposes.

At any meeting of the stockholders, the presence, in person or by proxy, of stockholders entitled to cast at least a majority of the votes which all stockholders are entitled to cast upon any matter shall constitute a quorum for the transaction of business upon such matter, and the stockholders present at a duly organized meeting can continue to do business until adjournment, notwithstanding the withdrawal of enough stockholders to leave less than a quorum. If a meeting cannot be organized because a quorum has not attended, those present may, except as otherwise provided by law, adjourn the meeting to such time and place as they may determine, but in the case of any meeting called for the election of directors, those who attend the second of such adjourned meetings, although less than a quorum, shall nevertheless constitute a quorum for the purpose of electing directors.

Except as otherwise provided in the Articles of Incorporation, as amended, or by law, every stockholder of record shall have the right, at every stockholders' meeting, to one vote for every share standing in his name on the books of the Company. In each election of directors, every stockholder entitled to vote shall have the right to multiply the number of votes to which he may be entitled by the total number of directors to be elected, and he may cast the whole number of such votes for one candidate or he may distribute them among any two or more candidates.

Every stockholder entitled to vote at a meeting of stockholders may authorize another person or persons to act for him by proxy. Every proxy shall be executed in writing by the stockholder or by his duly authorized attorney in fact and filed with the Secretary of the Company.

All questions shall be decided by the vote of the stockholders present, in person or by proxy, entitled to cast at least a majority of the votes which

all stockholders present are entitled to cast, unless otherwise provided by the Articles of Incorporation, as amended, or by law.

Elections for directors need not be by ballot except on demand made by a stockholder at the election and before the voting begins. In advance of any meeting of stockholders, the Board of Directors may appoint judges of election who need not be stockholders to act at such meeting or any adjournment thereof, and if such appointment is not made, the chairman of any such meeting may, and on request of any stockholder or his proxy shall, make such appointment at the meeting. The number of judges shall be one or three; and if appointed at a meeting on request of one or more stockholders or proxies, the majority of the shares present and entitled to vote shall determine whether one or three judges are to be appointed. No person who is a candidate for office shall act as a judge. In case any person appointed as judge fails to appear or fails or refuses to act, the vacancy may be filled by appointment made by the Board of Directors in advance of the convening of the meeting or at the meeting by the person or officer acting as chairman. On request of the chairman of the meeting or of any stockholder or his proxy, the judges shall make a report in writing of any challenge or question or matter determined by them and execute a certificate of any fact found by them.

ARTICLE III

Directors

SECTION 1. The business and affairs of the Company shall be managed by a Board of Directors. The directors need not be stockholders of the Company. The Board shall consist of not less than eight (8) nor more than eleven (11) directors, the exact number to be fixed from time to time by the Board of Directors pursuant to a resolution adopted by a majority vote of the directors then in office, such number being in addition to any directors that the holders of any class of preferred stock, voting as a class, may be entitled to elect as provided in the Articles of Incorporation, as amended, or in a resolution of the Board establishing any series of preferred stock.

The directors, other than the directors to be elected by the holders of No Par Preferred Stock, voting as a class, shall be classified in respect to the time for which they shall severally hold office by dividing them into three classes, each consisting, as nearly as possible, of one-third of the whole number of such directors. At each annual meeting, the successors to the class of directors whose terms expire that year shall be elected to hold office for the term of three years. Each such director shall hold office for the term for which he is elected and until his successor shall have been elected and qualified. Any vacancy in the office of any such directors shall be filled by an election by the Board for the unexpired term.

Directors to be elected by the holders of No Par Preferred Stock, voting as a class, shall be elected and hold office as provided in the Articles of Incorporation, as amended.

SECTION 2. The Board of Directors shall hold an annual meeting, without notice, immediately following the annual meeting of the stockholders and shall elect a President, such number of Vice Presidents and Operation or Division Presidents as the Board may deem advisable, a Secretary, a Treasurer, a Controller, and such Assistant Secretaries and Assistant Treasurers as the Board may deem advisable. The Board may also at its discretion elect a Chairman of the Board. Unless sooner removed by the Board, all officers shall hold office until the next annual meeting of the Board and until their successors shall have been elected. The Board shall also, from time to time, elect such other officers and agents as it deems advisable.

The President and the Chairman of the Board, if elected, must be selected from the members of the Board of Directors, but the other officers may but need not be directors.

Any two or more offices may be held by the same person except the offices of President and Secretary, but in no case shall the same person act in the same matter in two such official capacities.

SECTION 3. All vacancies in office shall be filled by the Board of Directors, and the Board shall have power to define the duties of all officers

and agents and fix their compensation and may remove at its discretion any officer or agent.

SECTION 4. The Board of Directors shall hold meetings at such times and places as it may determine. Directors may participate in a meeting of the Board or a Committee thereof by conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other. No notice of regular meetings of the Board need be given. Special meetings of the Board may be called by the President or a Vice President or the Secretary or by any two directors by giving written notice at least twenty-four hours in advance of the time of the meeting to each director, either personally or by telegram, charges prepaid, or by sending a copy of the notice through the mail at least two days before the day of the meeting, to the director's address appearing on the books of the Company or supplied by the director to the Company for the purpose of notice.

Attendance at any meeting of the Board shall be a waiver of notice thereof. If all the members of the Board are present at any meeting, no notice shall be required. A majority of the whole number of the directors shall constitute a quorum for the transaction of business, but if at any meeting a quorum shall not be present, the meeting may adjourn from time to time until a quorum shall be present.

SECTION 5. The Board of Directors shall cause to be sent to the stockholders, within 120 days after the close of each fiscal year, financial statements which shall include a balance sheet as of the close of such year, together with statements of income and surplus for such year, prepared so as to present fairly its financial condition and results of its operations. Such financial statements shall have been examined in accordance with generally accepted auditing standards by a firm of independent certified public accountants selected by the Board and shall be accompanied by such firm's opinion as to the fairness of the presentation thereof.

SECTION 6. The Board of Directors may, by resolution adopted by a majority of the whole Board, designate one or more committees, each committee to consist of two or more of the directors of the Company. The Board may designate one or more directors as alternate members of any committee, who may replace any absent or disqualified member at any meeting of the committee. Any such committee to the extent provided in such resolution shall have and exercise the authority of the Board in the management of the business and affairs of the Company.

ARTICLE IV

OFFICERS

President

SECTION 1. The President shall be the chief executive officer of the Company. He shall preside at all meetings of the stockholders and, in the absence of a Chairman of the Board, at all meetings of the Board of Directors at which he is present. He shall be ex-officio a member of all standing committees. He shall have the custody of the corporate seal or may entrust the same to the Secretary. He shall make reports of the Company's business to the Board at such times as the Board shall require. He shall perform all the usual duties incident to the office of President.

Vice-Presidents

SECTION 2. In the absence or disability of the President, his duties shall be performed by one or more Vice-Presidents designated by the Board of Directors. They shall perform such other duties as may be assigned to them by the Board.

Chairman of the Board

SECTION 3. The Chairman of the Board, if elected, shall preside at all meetings of the Board of Directors at which he is present. He shall perform such other duties as may be assigned to him by the Board.

Secretary

SECTION 4. The Secretary shall attend the meetings of the stockholders and Board of Directors and keep minutes thereof in suitable books. He shall send out notices of all meetings as required by law or these bylaws. He shall be ex-officio an Assistant Treasurer. He shall perform all the usual duties incident to the office of Secretary.

Assistant Secretaries

SECTION 5. In the absence or disability of the Secretary, his duties shall be performed by the Assistant Secretaries. They shall perform such other duties as may be assigned to them by the Board of Directors.

Treasurer

SECTION 6. The Treasurer shall have custody of funds of the Company and keep or cause to be kept accurate accounts of all money received or payments made in books kept for that purpose. He shall deposit all money received by him in the name and to the credit of the Company in such bank or other place or places of deposit as the Board of Directors shall designate. He shall be ex-officio an Assistant Secretary. He shall perform all the usual duties incident to the office of Treasurer.

Assistant Treasurers

SECTION 7. In the absence or disability of the Treasurer, his duties shall be performed by the Assistant Treasurers. They shall perform such other duties as may be assigned to them by the Board of Directors.

Controller

SECTION 8. The Controller shall have general charge of the accounting of the Company and shall perform all the usual duties incident to the office of Controller.

Bonds

SECTION 9. Such officers and employees of the Company as the Board of Directors shall determine shall give bond for the faithful discharge of their duties in such form and for such amount and with such surety or sureties as the Board shall require. The expense of procuring such bonds shall be borne by the Company.

ARTICLE V

Seal

The Company shall have a seal which shall contain the words "Armstrong World Industries, Inc.," in a circle within which the words "Incorporated Dec. 30, 1891" shall be contained.

ARTICLE VI

Stock Certificates and Transfers

Stock certificates shall be in such form as the Board of Directors may from time to time determine and shall either be signed by the President or one of the Vice-Presidents or other officer designated by the Board, and countersigned by the Treasurer or an Assistant Treasurer or other officer designated by the Board and sealed with the seal of the Company, or, if not so signed and sealed, shall bear the engraved or printed facsimile signatures of the officers authorized to sign and the engraved or printed facsimile of the seal of the Company.

The Board of Directors may appoint for any class of stock one or more incorporated banks or trust companies in the city of New York, New York, or elsewhere, to act as Registrar or Registrars, and also one or more incorporated banks or trust companies in the city of New York, New York, or elsewhere, to act as Transfer Agent or Transfer Agents. No certificate of stock of any class for which a Transfer Agent and Registrar have been

appointed shall be valid or binding unless countersigned by a Transfer Agent and registered by a Registrar before issue.

The shares of the capital stock of the Company shall, upon the surrender and cancellation of the certificate or certificates representing the same, be transferred upon the books of the Company at the request of the holder thereof, named in the surrendered certificate or certificates, in person or by his legal representatives or by his attorney duly authorized by written power of attorney filed with the Company's Transfer Agent. In case of loss or destruction of a certificate of stock, another may be issued in lieu thereof in such manner and upon such terms as the Board shall authorize.

The Board of Directors may fix a time, not more than seventy (70) days prior to the date of any meeting of the stockholders, or the date fixed for the payment of any dividend or distribution or the date for the allotment of rights, or the date when any change or conversion or exchange of capital stock will be made or go into effect, as a record date for the determination of the stockholders entitled to notice of, or to vote at, any such meeting, or entitled to receive payment of any such dividend or distribution, or to receive any such allotment of rights, or to exercise the rights in respect to any such change, conversion, or exchange of capital stock. In such case, only such stockholders as shall be stockholders of record on the date so fixed shall be entitled to notice of, or to vote at, such meeting, or to receive payment of such dividend or distribution, or to receive such allotment of rights, or exercise such rights, as the case may be, notwithstanding any transfer of stock on the books of the company after any record date fixed as aforesaid.

ARTICLE VII

Fiscal Year

The fiscal year of the Company shall end on the 31st day of December.

ARTICLE VIII

Amendments

Unless otherwise provided in the Articles of Incorporation, as amended, these bylaws may be amended by a vote of two-thirds of the members of the Board of Directors at any regular or special meeting duly convened after the notice of that purpose, subject always to the power of stockholders under law and in accordance with the Articles of Incorporation, as amended, to change such action.

ARTICLE IX

Limitation on Directors' Personal Liability; Indemnification of Directors and Officers

SECTION 1. A director of the Company shall not be personally liable for monetary damages for any action taken or failure to take any action unless the director has breached or failed to perform the duties of his or her office under Section 8363 of the Pennsylvania Directors' Liability Act and such breach or failure to perform constitutes self-dealing, willful misconduct or recklessness; provided, however, that the foregoing provision shall not eliminate or limit the liability of a director (i) for any responsibility or liability of such director pursuant to any criminal statute, or (ii) for any liability of a director for the payment of taxes pursuant to local, state or federal law.

SECTION 2. The Company shall indemnify to the full extent authorized or permitted by law any person made, or threatened to be made, a party to or otherwise involved in (as a witness or otherwise) an action, suit or proceeding (whether civil, criminal, administrative or investigative, and whether by or in the right of the Company or otherwise) by reason of the fact that the person is or was a director or officer of the Company or while a director or officer of the Company, either serves or served as a director, officer, trustee, employee or agent of any

other related enterprise or in connection with a related employee benefit plan at the request of the Company or serves or served as a director, officer, trustee, employee or agent of any other unrelated enterprise at the specific written request of the Company against any expenses and liability actually incurred including without limitation judgments and amounts paid or to be paid in settlement of and in actions brought by or in the right of the Company. Expenses incurred by such a person in defending a civil or criminal action, suit or proceeding or in enforcing any right under this Article shall be paid by the Company in advance of the final disposition of the action, suit or proceeding upon receipt of an undertaking by or on behalf of such person to repay such amount to the extent it shall ultimately be determined that such person is not entitled to be indemnified by the Company or, in the case of a criminal action, the majority of the Board of Directors so determines. The right to indemnification and advancement of expenses conferred in this Section shall not be deemed exclusive of any other rights to which any person indemnified may be entitled under any agreement, vote of stockholders or directors or otherwise, the Company having the express authority to enter such agreements as the Board of Directors deems appropriate for the indemnification of and advancement of expenses, including the creation of a fund therefor or equivalent guarantee, to present or future directors and officers of the Company in connection with their service as director or officer of the Company or their service as director, officer, trustee, employee or agent of any other enterprise or in connection with an employee benefit plan at the request of the Company. The right to indemnification and the advancement of expenses provided in this Section shall be a contract right, shall continue as to a person who has ceased to serve in the capacities described herein, and shall inure to the benefit of the heirs, executors and administrators of such person.

SECTION 3. No amendment, alteration or repeal of this Article IX, nor the adoption of any provision inconsistent with this Article IX, shall adversely affect any limitation on the personal liability of a director or officer, or the rights of a director or officer to indemnification and advancement of expenses, existing at the time of such amendment, modification or repeal, or the adoption

of such an inconsistent provision.

EXHIBIT NO. 10(i)(a)

**AGREEMENT CONCERNING
ASBESTOS-RELATED CLAIMS**

June 19, 1985

AGREEMENT CONCERNING ASBESTOS-RELATED CLAIMS

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AGREEMENT CONCERNING ASBESTOS-RELATED CLAIMS

This Agreement to provide for the administration, defense, payment and disposition of asbestos-related claims (hereinbelow referred to as the "Agreement") is made between and among the Subscribing Producers, as defined hereinbelow, and the Subscribing Insurers, as defined hereinbelow.

WITNESSETH:

WHEREAS, Subscribing Producers and Subscribing Insurers have considered the nature of asbestos-related claims, their number and widespread distribution throughout the United States, the various rules of law governing their resolution, the scope and complexity of the insurance arrangements related thereto, and the burden that such claims have placed on the American civil justice system; and

WHEREAS, Subscribing Producers and Subscribing Insurers recognize the existence of numerous insurance coverage disputes between and among Insurers and Producers, differing court decisions, and the existence of cross-actions among Producers and among Insurers; and

WHEREAS, Subscribing Producers and Subscribing Insurers desire to simplify the procedures for handling claims, reduce the costs of such procedures, apply insurance arrangements in a consistent manner and take other steps reasonable and practical to ensure the expenditure of funds for the reasonable payment of meritorious claims at reasonable processing costs; and

WHEREAS, Subscribing Producers and Subscribing Insurers desire to resolve and discontinue the various disputes concerning insurance coverage for asbestos-related claims and to embark upon a method for resolution of asbestos-related claims and the insurance arrangements pertaining thereto;

NOW THEREFORE, in consideration of the mutual covenants herein contained and intending to be legally bound hereby, the Subscribing Producers and Subscribing Insurers hereby agree as follows:

I. GENERAL CONDITIONS

1. Any Producer or Insurer may become a signatory to the Agreement on or before June 19, 1985, and in so doing shall agree to be bound by the terms and conditions of the Agreement and the Appendices hereto, and prior to said date shall offer participation in the Agreement to each and every of its Producers or Insurers, as the case may be. If a Producer or Insurer does not become a signatory hereto on or before June 19, 1985, but subsequently wants to become a signatory as a result of changed circumstances, participation in the Agreement by such Producer or Insurer may be in conflict with the fixed commitments and compromises upon the basis of which other Producers and Insurers will have entered into the Agreement on or before June 19, 1985. Participation in the Agreement by additional proposed signatories therefore shall be considered only in accordance with Section XXI hereinbelow.

2. The Agreement is intended to apply solely to asbestos-related claims, as defined hereinbelow. It is the product of informed negotiations among the signatories hereto, involving compromises of previously stated legal positions. The Agreement does not necessarily reflect the views of

Subscribing Producers and Subscribing Insurers as to their rights and obligations with regard to matters or persons outside of the scope of the Agreement, and with respect to all such matters or persons, all signatories reserve all previously held positions and all other rights and privileges.

3. The Agreement is intended to confer rights and benefits only upon Subscribing Producers and Subscribing Insurers, and is not intended to confer any rights or benefits upon persons not signatories to the Agreement. No person other than a signatory hereto shall have any legally enforceable rights under the Agreement. All rights of action for any breach of this Agreement by any signatory hereto are hereby reserved to Subscribing Producers and Subscribing Insurers.

4. All actions taken and statements made by persons or their representatives relating to their participation in the Agreement, including its development and implementation, shall be without prejudice or value as precedents, and shall not be taken as a standard by which other matters may be judged.

5. All persons subscribing to or otherwise associating themselves with the Agreement request all Courts to take notice of its underlying purpose, and to accord all persons subscribing to or otherwise associating themselves with the Agreement and their representatives full privilege and protection with respect to the disclosure of their actions, statements, documents, papers and other materials relating to the Agreement, including its development and implementation.

II. ESTABLISHMENT OF FACILITY

1. Subscribing Producers and Subscribing Insurers shall establish a non-profit organization to be known as the Asbestos Claims Facility (hereinafter referred to as the "Facility"). The Facility shall administer and arrange for the evaluation, settlement, payment or defense of all asbestos-related claims against Subscribing Producers and Subscribing Insurers in accordance with the provisions of the Agreement and Appendix A hereto, and pursuant to the provisions of law and professional standards applicable to Subscribing Insurers.

2. The Facility shall be governed by a Board of Directors whose members shall number at least 12 and whose members shall contain an equal number of representatives of Subscribing Producer members and of Subscribing Insurer members. The Board of Directors shall have power to increase the number of directors and to add public directors, to appoint such officers, employees and committees of persons as the Board sees fit, to define their authorities and responsibilities and to set the conditions of their appointments. The Board of Directors shall have no power to modify any provisions of the Agreement or of the Appendices hereto.

3. The Facility shall not sell, lease, exchange, mortgage, pledge, or otherwise dispose of all or substantially all of its property or assets and shall not dissolve or wind up its affairs except upon the affirmative vote of two-thirds of Subscribing Producer members with two-thirds interest or two-thirds of Subscribing Insurer members with two-thirds interest.

III. MEMBERSHIP IN FACILITY

1. Subject to the provisions of Section XXI hereinbelow, each Producer and each Insurer shall become a member of the Facility upon becoming a signatory to the Agreement and shall invite each of its Producers or

Insurers, as the case may be, to become a signatory to the Agreement and thereby to become a member of the Facility.

2. Voting rights of members and voting procedures shall be determined respectively by Subscribing Producers and Subscribing Insurers.

3. Neither the Board of Directors nor any other persons shall have any authority to terminate the membership of a member without the consent of such member; provided, that membership in the Facility shall terminate at such time as a member no longer has an obligation to make payments or to pay expenses pursuant to the Agreement and the Appendices hereto. A member may terminate its membership in the Facility at any time upon written notice to the Facility, but, except as otherwise explicitly provided herein, termination of membership shall not modify the rights and obligations of a Subscribing Producer, Subscribing Insurer or the Facility under the Agreement and the Appendices hereto.

IV. SUBMISSION AND WITHDRAWAL OF CLAIMS

1. By becoming a signatory to the Agreement, each Subscribing Producer and each Subscribing Insurer designates the Facility as its sole agent to administer and arrange on its behalf for the evaluation, settlement, payment or defense of all asbestos-related claims against such Subscribing Producer or Subscribing Insurer. As sole agent, the Facility shall have exclusive authority and discretion to administer, evaluate, settle, pay or defend all asbestos-related claims. Except as otherwise provided in Paragraph 2 hereinbelow, the Facility shall serve perpetually as the sole agent of each Subscribing Producer and each Subscribing Insurer with respect to all asbestos-related claims.

2. Any Subscribing Producer or Subscribing Insurer may withdraw the designation of the Facility as its sole agent made pursuant to Paragraph 2 hereinabove, and may terminate the Facility's right and authority to act on behalf of such Subscribing Producer or Subscribing Insurer by providing written notice to the Facility 60 days prior to the effective date of such withdrawal; provided, that such withdrawal shall apply only to asbestos-related claims filed or made against the withdrawing Subscribing Producer or Subscribing Insurer subsequent to the effective date of withdrawal. The Facility shall continue to serve as sole agent for such Subscribing Producer or Subscribing Insurer with respect to all asbestos-related claims filed on or before the effective date of withdrawal.

V. COOPERATION WITH FACILITY

Each Subscribing Producer and each Subscribing Insurer shall comply with the terms and conditions of the Agreement and the Appendices hereto, and shall cooperate with and assist the Facility in furtherance of such terms and conditions. Each Subscribing Producer and each Subscribing Insurer shall respond fully and in a timely manner to reasonable requests by the Facility for information and shall assist in the securing and giving of evidence concerning asbestos-related claims. To the extent practicable, the Facility shall maintain the confidentiality of confidential or proprietary information submitted by Subscribing Producers and Subscribing Insurers.

VI. ALLOCATION OF LIABILITIES AND EXPENSES

1. Liability payments and allocated expenses shall be allocated to each Subscribing Producer on the date such Producer becomes a signatory to the Agreement. Such allocation shall establish the responsibility of each Subscribing Producer for a percentage of liability payments and a percentage of allocated expenses attributable to each claim handled by the Facility as sole agent for such Subscribing Producer under Section IV hereinabove. Each Subscribing Producer's percentages of liability payments and allocated expenses shall be established as provided in Appendix A-1 hereto, and shall be subject to modification only in the manner and to the extent set forth therein. To the extent that a Subscribing Producer's percentages of liability payments and allocated expenses attributable to a particular asbestos-related claim are not payable by one or more Subscribing Insurers pursuant to the Agreement and the Appendices hereto, such Subscribing Producer shall pay the percentages of liability payments and allocated expenses in question.

2. Each Subscribing Insurer shall acquiesce in and abide by the allocation of percentages of liability payments and allocated expenses to each Subscribing Producer, as described in Paragraph 1 hereinabove, and shall consider, recognize and hold each Subscribing Producer's shares of liability payments and allocated expenses attributable to each asbestos-related claim to be necessary, reasonable and proper and each Subscribing Producer to be properly bound and obligated to pay such sums. Each Subscribing Insurer shall pay a share of unallocated expenses and start-up costs as provided in Appendix A-2 hereto, which shall be subject to modification only in the manner and to the extent set forth therein.

VII. FACILITY CLAIMS HANDLING

1. Except as otherwise provided in Section IV hereinabove, the Facility shall administer, evaluate, settle, pay or defend all asbestos-related claims against Subscribing Producers and Subscribing Insurers, either within the Facility's procedures or through standard judicial means. The Facility shall handle each asbestos-related claim on behalf of all Subscribing Producers and Subscribing Insurers, and shall not settle an asbestos-related claim on behalf of fewer than all Subscribing Producers and Subscribing Insurers. The Facility shall settle each asbestos-related claim so as to extinguish claims for all damages, including punitive damages, and, in the settlement of asbestos-related claims, the Facility shall not pay punitive damages to claimants.

2. The Facility shall hire competent and experienced legal counsel to defend asbestos-related claims and shall retain such counsel as are necessary and appropriate to defend the interests of Subscribing Producers. The Facility may use its employees and independent persons to provide professional medical and other assistance and advice.

3. Actions against nonsubscribing persons may be undertaken by the Facility on behalf of Subscribing Producers and Subscribing Insurers, but the Agreement shall neither require nor preclude such actions.

4. The Facility shall require valid evidence to support each claim against Subscribing Producers and Subscribing Insurers, and shall require credible medical evidence in each case prior to making payment to a claimant. Facility personnel shall be responsible for obtaining such evidence from each claimant and verifying it.

5. A claimant shall be paid solely for asbestos-related physical impairment and dysfunction. If such claimant subsequently develops an asbestos-related malignancy, the claimant may submit a subsequent claim. In addition, the Facility may provide certain claimants whose claims have not matured with an opportunity to resubmit a claim to the Facility should additional medical evidence become available. The Facility may enter into agreements to suspend the running of statutes of limitations with respect to claims timely presented and shall adopt uniform, streamlined, expeditious procedures, including voluntary nonjudicial means of resolving disputed claims.

6. Each asbestos-related claim shall be evaluated on its individual merits, but this shall not preclude two or more asbestos-related claims from being settled simultaneously.

7. The Facility shall not make payments pursuant to a pre-determined schedule of benefits, but detailed claims guidelines shall be used to evaluate and settle asbestos-related claims. The Facility shall make payments and settle claims only on behalf of Subscribing Producers and Subscribing Insurers and shall be entitled to credit for settlements made and judgments paid by Subscribing Producers and Subscribing Insurers prior to subscription in the Facility.

8. The Facility shall operate according to annual liability, defense and operational programs to be established by the Board of Directors. The Facility shall be subject to annual financial and quality control audits by persons selected by the Board of Directors and consisting of an equal number of representatives of Subscribing Producers and of Subscribing Insurers.

VIII. COVERAGE DISPUTES AND WAIVERS OF CLAIMS AND DEFENSES

1. Each Subscribing Producer and each Subscribing Insurer shall forgo all claims for declaratory relief or damages, as to other Subscribing Producers and Subscribing Insurers, relating to the application of insurance to the investigation, settlement, defense or indemnification of asbestos-related claims within the scope of the Agreement. Upon becoming a signatory to the Agreement, all such claims shall be withdrawn and dismissed from pending actions, as to Subscribing Producers and Subscribing Insurers, with prejudice and without delay.

2. Each Subscribing Producer and each Subscribing Insurer shall forgo all claims for contribution or indemnity (other than for contribution or indemnity assumed under written agreement) against other Subscribing Producers and Subscribing Insurers with respect to all asbestos-related claims except those claims with respect to which a Subscribing Producer or Subscribing Insurer has withdrawn pursuant to Section IV hereinabove.

3. Each Subscribing Producer and each Subscribing Insurer shall waive claims for bad faith or punitive damages, as to other Subscribing Producers

and Subscribing Insurers, with respect to all matters within the scope of the Agreement; provided, that this waiver shall not apply to claims, including punitive damages, for breach of or bad faith with respect to the Agreement.

4. This Section VIII shall not preclude a Subscribing Producer or Subscribing Insurer from seeking reimbursement under other provisions of the Agreement. In addition, there are a limited number of issues with respect to which the possibility of litigation is specifically provided for herein, but, except as otherwise provided in Paragraph 3 hereinabove, all claims for bad faith or punitive damages, as to other Subscribing Producers and Subscribing Insurers, shall be waived in such litigation.

5. Except as otherwise provided in Appendix B hereto, each Subscribing Insurer shall waive and permanently abandon and shall not assert or apply any conditions or defenses based upon, or exclusionary provisions contained in, insurance policies, which defenses or provisions have the effect of reducing or denying insurance coverage available under any of the insurance policies issued by Subscribing Insurers to Subscribing Producers. This waiver includes clauses in multiple insurance policies issued by the same insurer that seek to shift the entire loss arising out of one occurrence to one of the insurance policies or to reduce the amounts payable under one insurance policy with respect to the entire loss by amounts paid under any one of the other insurance policies.

6. Subscribing Producers and Subscribing Insurers shall resolve through alternative dispute resolution, in the manner set forth in Appendix C hereto, any disputed issues within the scope of the Agreement and the Appendices hereto.

IX. COVERAGE BLOCK AND FUNDING

1. The "coverage block," with respect to each Subscribing Producer, consists of all insurance policies issued to such Subscribing Producer by its Subscribing Insurers to become effective prior to the date (within the period January 1, 1973 through December 31, 1979) selected by the Producer and set forth in its Schedules of Insurance and, except as set forth hereinbelow, shall not include any periods subsequent to said date; provided, that the coverage block shall not begin prior to the date of said Producer's first involvement with asbestos or asbestos-containing products. Insurance policies written to become effective prior to June 19, 1985, and subsequent to the ending date of a Subscribing Producer's initial coverage block may be added consecutively (by year with respect to annual limits) to such coverage block by payment, as due, of any applicable deductibles, retrospective rating premiums or self-insured retentions in accordance with the provisions of Sections XV and XVI hereinbelow and subject to appropriate credit for amounts previously paid by the Producer on account of such deductibles, retrospective rating premiums or self-insured retentions. Such insurance policies, when added, become part of the Producer's coverage block. Uninsured periods likewise may be consecutively added, and must be added if they fall between consecutively added insured periods; provided, that if a Producer adds a period for which it did not purchase insurance subsequent to the initial coverage block, such Producer shall make liability payments and pay allocated expenses for that period.

2. The "exposure period," with respect to each asbestos-related claim for a particular injury, is the period from a person's first exposure to any asbestos or asbestos-containing products until first diagnosis of such injury or death resulting from such injury, whichever occurs first.
3. Any insurance policies covering a part of the exposure period for a particular claim may be used to make liability payments and to pay allocated expenses for such claim in accordance with the provisions of this Section IX, in the manner set forth in Sections X and XI hereinbelow.
4. An insurance policy of an insolvent Subscribing Insurer shall be treated as would any uninsured period in the initial coverage block; provided, that with respect to an insolvent London Company (exclusive of Lloyds syndicate members) that has underwritten a share within a particular insurance policy, the Subscribing Producer in question shall pay such insolvent Company's share of payments required under the insurance policy pursuant to the Agreement.
5. Insurance policies that expressly provide coverage on a specific manifestation or claims-made basis or first discovery trigger shall be included within the coverage block in a manner consistent with their terms.
6. Neither the insurance policies comprising a Subscribing Producer's coverage block nor any other insurance policies set forth in the Producer's Schedules of Insurance are dedicated solely to asbestos-related claims, and they may be used for the administration, handling or disposition of any other claims covered thereunder and, subject to the terms and conditions of the insurance policy in question, payments shall apply toward the exhaustion of any applicable insurance policy limits.
7. With respect to each Subscribing Producer, all liability payments and allocated expenses arising out of the products hazard or completed operations hazard, as defined in the insurance policy in question, shall be covered exclusively by products coverage (subject to applicable aggregate limits if any), notwithstanding the presence of allegations such as, but not limited to, strict liability, failure to warn, negligence, breach of warranty, fraud, misrepresentation, concealment or conspiracy.

X. LIABILITY PAYMENTS

With respect to a particular asbestos-related claim, liability payments attributable to such claim for each Subscribing Producer shall be made as provided hereinbelow:

1. Subject to the provisions of Section XX hereinbelow, each primary insurance policy in the coverage block that covers any part of the exposure period shall make liability payments; and each excess insurance policy in the coverage block that covers any part of the exposure period not then covered by underlying primary or excess insurance in the coverage block also shall make liability payments; provided, that no insurance policy shall make liability payments after its limits of liability have been exhausted. Except as otherwise provided herein, whenever a Subscribing Producer has no insurance for a particular period within the coverage block, liability payments

otherwise allocable to that period shall be allocated pursuant to Paragraph 2 hereinbelow to the periods within the coverage block for which the Subscribing Producer has insurance and to periods added to the coverage block for which the Subscribing Producer did not purchase insurance.

2. The amount of liability payments to be made by each insurance policy described in Paragraph 1 hereinabove shall bear the same relation to the aggregate liability payments incurred as the part of the exposure period then covered by such insurance policy bears to the total parts of the exposure period then covered by insurance policies in the coverage block and by periods added to the coverage block for which the Subscribing Producer did not purchase insurance; provided, that a Subscribing Producer shall make liability payments only if no part of the exposure period is then covered by insurance policies in the coverage block, except as otherwise provided herein.

XI. ALLOCATED EXPENSES

With respect to a particular asbestos-related claim, allocated expenses attributable to such claim for each Subscribing Producer shall be paid as provided hereinbelow:

1. Subject to the provisions of Section XX hereinbelow, unless it expressly provides otherwise, each primary insurance policy in the coverage block that covers any part of the exposure period shall pay allocated expenses; and, unless it expressly provides otherwise, each excess insurance policy in the coverage block that covers any part of the exposure period not then covered by underlying primary or excess insurance in the coverage block also shall pay allocated expenses; provided, that such excess insurance policy shall only pay allocated expenses where: A) payment of allocated expenses would not apply against the aggregate limits of such excess insurance policy; or B) no primary insurance policies in the coverage block cover a part of the exposure period; or C) remaining primary insurance policies cover 10 percent or less of the period comprising the coverage block initially selected by the Subscribing Producer; or D) the initial coverage block is less than ten years and only one primary policy year remains within the coverage block. Except as otherwise provided herein, whenever a Subscribing Producer has no insurance paying allocated expenses for a particular period within the coverage block, allocated expenses otherwise allocable to that period shall be allocated to the periods within the coverage block for which the Subscribing Producer has insurance paying allocated expenses and to periods added to the coverage block for which the Subscribing Producer did not purchase insurance.

2. The amount of allocated expenses to be paid by each insurance policy paying allocated expenses pursuant to Paragraph 1 hereinabove shall bear the same relation to the aggregate allocated expenses incurred as the part of the exposure period then covered by such insurance policy bears to the total parts of the exposure period then covered by insurance policies in the coverage block paying allocated expenses and by periods added to the coverage block for which the Subscribing Producer did not purchase insurance; provided, that a Subscribing Producer shall pay allocated expenses only if no part of the

exposure period is covered by insurance policies in the coverage block paying allocated expenses, except as otherwise provided herein.

3. The payment of allocated expenses shall not apply against the aggregate limits of primary insurance policies unless the insurance policies in question expressly provide otherwise. The payment of allocated expenses shall apply against the aggregate limits of excess insurance policies unless the insurance policies in question expressly provide otherwise; provided, that with respect to excess insurance policies that expressly follow the provisions of underlying insurance policies for the payment of allocated expenses, such underlying language shall apply except where it is inconsistent with the terms and conditions of the excess insurance policy.

XII. PAYMENT OF ALLOCATED AND UNALLOCATED EXPENSES FOLLOWING EXHAUSTION OF LIMITS

1. Each Subscribing Insurer, with respect both to policies of insurance that expressly provide that the duty to defend ceases upon exhaustion of aggregate limits (generally, post-1966 standard form insurance policies) and to pre-1966 standard form insurance policies, shall pay allocated and unallocated expenses until its limits of liability are exhausted but not thereafter.

2. As to Subscribing Producers whose asbestos-related claims are being administered by the Facility, Subscribing Insurers that have issued pre-1966 standard form insurance policies shall establish, administer and fund an Insurance Defense Program, as set forth in Appendix E hereto, to cover the allocated and unallocated expenses of all claims that under the Agreement would have triggered a pre-1966 standard form insurance policy. The Insurance Defense Program, on behalf of Subscribing Insurers that have issued pre-1966 standard form insurance policies, shall respond, as would any insurance policy paying allocated expenses under the Agreement, to pay allocated and unallocated expenses for any claim triggering a pre-1966 standard form insurance policy year where: A) there is no obligation in such policy year to pay allocated expenses for such claim; and B) no other insurance policies are paying allocated expenses for such claim or the payment of allocated expenses by any of the insurance policies paying allocated expenses for such claim applies against aggregate limits pursuant to Section XI hereinabove or the Subscribing Producer is paying allocated expenses for such claim. The Insurance Defense Program shall not be taken into account in determining whether an excess insurance policy pays allocated expenses pursuant to Paragraph 1 of Section XI hereinabove.

XIII. START-UP COSTS OF FACILITY

1. All start-up costs shall be paid by Subscribing Primary Insurers in accordance with Appendix A-2 hereto.

2. Charter subscribers may mitigate the start-up expense burden through entrance fees that shall be charged to new subscribers in accordance with Appendix A-2 hereto; provided, that new subscribers do not include Subscribing Producers, except in the case of a new Producer with no Subscribing Insurers.

XIV. UNALLOCATED EXPENSES OF FACILITY

1. All unallocated expenses of the Facility shall be paid by Subscribing Primary Insurers and Subscribing Excess Insurers as they are called upon to make payments within the terms of the Agreement, as described more fully in Appendix A-2 hereto.
2. A Subscribing Insurer shall be relieved of the obligation to pay unallocated expenses upon the exhaustion of all of its obligations to make liability payments and to pay allocated expenses.
3. A Subscribing Producer shall be obligated to pay a share of Facility unallocated expenses only after all applicable insurance within the coverage block is exhausted.

XV. DEDUCTIBLES AND RETROSPECTIVE RATING PLANS

1. When a Subscribing Producer includes within its coverage block a particular period of insurance subject to a deductible, self-insured retention or retrospective rating plan under which payment would be due from such Subscribing Producer, that Subscribing Producer shall pay the deductible, self-insured retention or retrospective rating premium as due, except as otherwise provided herein.
2. A "date" shall be mutually agreed upon by each Subscribing Producer and its Subscribing Insurers for purposes of this Section XV and Sections XVI and XVII hereinbelow. The agreed-upon date may be the same as or different from the date unilaterally selected by the Subscribing Producer for the purpose of defining its coverage block pursuant to Section IX hereinabove. All insurance policies issued to a Subscribing Producer prior to the mutually agreed-upon date are "pre-date" insurance policies. All insurance policies issued to a Subscribing Producer subsequent to the mutually agreed-upon date are "post-date" insurance policies.
3. All deductibles and retentions, whether in pre-date or post-date insurance policies, shall be applied in a pro-rata manner in the same proportion as the policy year is called upon to make liability payments.
4. Once retrospective rating plans have been closed, whether prior to or following the date a person becomes a signatory to this Agreement, they shall not require any additional payments by a Subscribing Producer.
5. Unless otherwise explicitly provided in the insurance policy in question, payment by a Subscribing Producer of a deductible shall not reduce the aggregate limits of such insurance policy.
6. With respect to a primary insurance policy containing a clause or endorsement providing substantially that payments made which include a deductible amount shall not increase the Insurer's liability with respect to each occurrence and aggregate, once the Subscribing Producer or the Subscribing Primary Insurer has paid an amount equal to the aggregate limits, the Subscribing Producer shall pay no more on account of such deductible and

the Subscribing Primary. Insurer and Subscribing Excess Insurer shall resolve between themselves the responsibility for payments for such year.

XVI. APPLICATION OF INSURANCE POLICIES WITHOUT DEDUCTIBLE OR RETENTION LIMITS

A. PRE-DATE INSURANCE POLICIES

1. Where deductibles and retentions are not limited explicitly by the insurance policy language, the following schedule of multipliers shall apply to limit per policy year such deductibles and retentions:

Face Amount of Deductible or Retention -----	Multiplier -----	Policy Year Cumulative Maximum -----
Up to \$5,000	10	\$ 50,000
Next \$20,000	7.5	\$200,000

2. With respect to per claim deductibles in excess of \$25,000, the maximum to be paid for each policy year by a Subscribing Producer is the aggregate limit of the deductible-containing insurance policy. With respect to per occurrence deductibles in excess of \$25,000, the affected parties shall resolve disagreements by negotiation, followed by non-binding alternative dispute resolution, followed, if necessary, by litigation. Any such resolution shall apply, in all respects, to the affected parties notwithstanding any other provisions of the Agreement.

3. Where an insurance policy containing a deductible explicitly provides that payment of deductibles reduces aggregate limits, then payment of deductibles shall apply against aggregate limits, following the exhaustion of which, excess insurance policies shall become available. In all other cases involving deductibles, payment of deductibles shall not apply against aggregate limits, and excess insurance shall become available after the underlying insurance policy has paid its remaining limits.

B. POST-DATE INSURANCE POLICIES

1. Deductibles and retentions shall apply as written. Affected parties shall resolve any disagreements by negotiation, followed by non-binding alternative dispute resolution, followed, if necessary, by litigation. Any such resolution shall apply, in all respects, to the affected parties notwithstanding any other provisions of the Agreement.

2. With respect to deductibles or retentions in an insurance policy underlying an excess insurance policy that contains standard excess ultimate net loss and/or loss payable clauses, such excess insurance policy shall respond when liability payments equivalent to the amount of the aggregate limits of the underlying insurance policy in question have been made by the Subscribing Producer or the Subscribing Insurer or both, unless:

(A) There is evidence that the Subscribing Excess Insurer was aware of the uncapped deductible or retention when writing its insurance policy, such evidence to be in: (1) the schedule of insurance in the excess insurance policy; (2) the underwriting file of the Subscribing Excess Insurer; (3) the underwriter's placing slip; or (4) the underwriting file of the London broker (not any American broker); and

(B) Such evidence is provided to the Producer by the Excess Insurer within 60 days of March 29, 1985, or of the date that the excess insurance policy in question is listed in the Producer's Schedules of Insurance provided to such Excess Insurer, whichever occurs later.

XVII. APPLICATION OF INSURANCE POLICIES WITHOUT AGGREGATE LIMITS

A. PRE-DATE INSURANCE POLICIES

1. With respect to (A) primary products liability coverage written without aggregate limits either inadvertently or before the aggregate concept was developed, (B) primary non-products liability coverage written without aggregate limits at any time, and (C) in the coverage for any particular year the first excess occurrence policy without aggregate limits written directly above an insurance policy with aggregate limits, the following schedule of multipliers shall apply per policy year to provide aggregate limits for such policies:

Face Amount of Per Occurrence/Accident Limits	Multiplier	Policy Year Cumulative Maximum
Up to \$100,000.....	10	\$1,000,000
Next \$200,000.....	5	\$2,000,000
Next \$200,000.....	3	\$2,600,000
Next \$500,000.....	1.5	\$3,350,000

Above \$1,000,000..... 1 N/A

In addition, upon exhaustion of all applicable insurance policies for the year in question, the no-aggregate primary insurance policy shall respond with coverage equal to ten times the per occurrence/accident limits up to the first \$1 million of the per occurrence/accident limits, minus amounts previously applied to the maximum limit of such insurance policy.

2. All other primary products liability coverage written without aggregate limits shall apply as written. In the event of a dispute, affected parties shall engage in negotiation, followed by non-binding alternative dispute resolution, followed, if necessary, by litigation. Any such resolution shall apply, in all respects, to the affected parties notwithstanding any other provisions of the Agreement.

3. All other excess occurrence policies without aggregate limits shall apply to the extent of one per occurrence/accident limit.

B. POST-DATE INSURANCE POLICIES

Post-date insurance policies without aggregate limits shall apply as written. In the event of a dispute, affected parties shall engage in negotiation, followed by non-binding alternative dispute resolution, followed, if necessary, by litigation. Any such resolution shall apply, in all respects, to the affected parties notwithstanding any other provisions of the Agreement.

XVIII. POLICY PERIODS OF OTHER THAN 12 MONTH MULTIPLES

1. Unless it expressly provides otherwise, an insurance policy of less than 12 months shall carry full aggregate limits for the term of such policy.

2. Absent agreement among the affected parties, unless the insurance policy or other documentary evidence explicitly provides that another result was intended:

(A) Where an insurance policy was extended prior to the expiration date for a period other than a multiple of 12 months: (1) if the extension was at the request of the Subscribing Producer, the period of less than 12 months shall carry pro-rata limits; and (2) if the extension was at the request of the Subscribing Insurer, the period of less than 12 months shall carry full aggregate limits;

(B) Where an insurance policy was initially written for more than one year but not for a multiple of 12 months, then the period of less than 12 months also shall carry full aggregate limits; and

(C) Where an insurance policy was canceled prior to the expiration date by either the Subscribing Producer or Subscribing Insurer, then the period of less than 12 months shall carry full aggregate limits, except where a Subscribing Excess Insurer canceled its insurance policy specifically to make its insurance policies concurrent with underlying insurance policies and the Subscribing Producer agreed, in which case the period of less than 12 months shall carry pro rata limits.

3. Deductibles and retentions in insurance policies described in this Section XVIII shall apply in a manner consistent with the application of limits hereunder.

XIX. RETROSPECTIVE AND PROSPECTIVE APPLICATION

1. Except as otherwise provided in Section XXI hereinbelow, any and all provisions of the Agreement shall apply, as between a Subscribing Producer and Subscribing Insurer, to all liability payments and expenses incurred subsequent to the date on which both the Subscribing Producer and Subscribing Insurer became signatories to the Agreement, and with respect thereto and to the extent inconsistent herewith, shall nullify, repudiate, replace and supplant, as between such Subscribing Producer and Subscribing Insurer, any prior agreements or judicial determinations whether or not final; provided,

that this Paragraph shall not apply to the extent that a Subscribing Insurer, by written agreement executed prior to March 29, 1985, extinguished or exhausted an insurance coverage obligation by payment of monies to a Subscribing Producer or affiliated company. With respect to such extinguishment of an insurance coverage obligation, the Subscribing Producer in question shall make liability payments and pay expenses (including payments due under Appendix E) as would the Subscribing Insurer in question under the Agreement in the absence of such extinguishment, and the Subscribing Producer shall make such payments and pay such expenses until the Subscribing Producer has paid hereunder an amount equal to the monies received from such Subscribing Insurer with respect to such extinguishment., plus investment income, if any, on such monies, and less any payments made and expenses paid directly by such Subscribing Producer for asbestos-related claims.

2. Subject to the provisions of this Section XIX, and except as otherwise provided hereinbelow in this Paragraph 2, each Subscribing Producer and each Subscribing Insurer shall be reimbursed for liability payments and allocated and unallocated expenses, including deductibles, retrospective premiums and loss conversion factors, incurred prior to the date on which the Subscribing Producer or Subscribing Insurer became a signatory to the Agreement, such reimbursement to be made in accordance with the Agreement and as if the Agreement (but not Section VI or Appendix A-1) were in effect at the time such payments and expenses initially were incurred; provided, that payments and expenses incurred pursuant to an agreement explicitly providing that such payments are final or to a final settlement agreement or final judicial determination that became effective prior to the date on which the Subscribing Producer or Subscribing Insurer became a signatory to the Agreement shall not be subject to reimbursement or reallocation. Notwithstanding the provisions of Section XX hereinbelow, neither a Subscribing Producer nor a Subscribing Insurer shall make reimbursements for amounts that otherwise would have been reimbursed hereunder by an Insurer not a signatory hereto if said Insurer had become a signatory hereto.

3. Reimbursement of payments and expenses due hereunder shall be made within 90 days of the date the Subscribing Producer or Subscribing Insurer became a signatory to the Agreement. At the option of such Producer or Insurer, reimbursement of payments and expenses may be made quarterly in not more than twelve equal consecutive installments from the date payable under the Agreement, with interest upon any unpaid principal balances compounded daily and payable on a quarterly basis at the rate of interest announced publicly by Citibank, N.A., in New York, New York, from time to time as Citibank, N.A.'s Base Rate.

4. Reimbursement of payments and expenses pursuant to Paragraph 2 hereinabove shall be made by and reallocated among primary and excess insurance policies in a reasonable manner, and shall not require reallocation on an individual case basis.

5. With respect to fees and expenses incurred in asbestos insurance coverage litigation, each Subscribing Producer and each Subscribing Insurer, in the absence of agreement, may submit claims for such fees and expenses to alternative dispute resolution.

6. A Subscribing Producer shall not be reimbursed for allocated or unallocated expenses incurred in fulfilling its duty of assistance and cooperation under its insurance policies:

(A) In-house costs claimed by a Subscribing Producer to be in excess of those incurred in fulfilling its duty of assistance and cooperation under its insurance policies, in the absence of agreement with its Subscribing Insurers, may be submitted to alternative dispute resolution; and

(B) Claims by a Subscribing Producer for fees and expenses incurred for coordinating counsel, in the absence of agreement with its Subscribing Insurers, may be submitted to alternative dispute resolution.

XX. INSURANCE ISSUED BY NON-SIGNATORIES

1. Whenever a Subscribing Producer has an insurance policy issued to it for a particular period within the coverage block by an Insurer that is not a signatory hereto, such Producer shall use its reasonable best efforts, including, if necessary, the timely pursuit of litigation, to obtain a final and reasonable settlement agreement or final judicial determination concerning the application of such insurance policy to asbestos-related claims. With respect thereto, each Subscribing Producer and each Subscribing Insurer, to the extent practicable, shall cooperate with and assist the Subscribing Producer in question.

2. Whenever, with respect to an insurance policy described in Paragraph 1 hereinabove, the Subscribing Producer, pursuant to a final settlement agreement or final judicial determination, has received from the Insurer in question monies to administer, handle or dispose of asbestos-related claims, such Subscribing Producer shall make payments and pay expenses (including payments due under Appendix E) as would the Insurer in question with respect to such Producer if said Insurer had become a signatory hereto, and the Subscribing Producer shall make such payments and pay such expenses until the Subscribing Producer has paid an amount equal to the monies received from such Insurer to administer, handle or dispose of asbestos-related claims plus investment income, if any, on such monies and less proration of any payments made and unreimbursed expenses paid directly by such Subscribing Producer for asbestos-related claims or incurred in obtaining such judicial determination or settlement agreement.

3. Whenever an insurance policy described in Paragraph 1 hereinabove would have had to make payments or to pay expenses on a particular claim under the Agreement had the Insurer in question become a signatory hereto, and the Subscribing Producer has not received monies from such non-signatory Insurer pursuant to Paragraphs 1 and 2 hereinabove, each insurance policy in the coverage block covering a part of the exposure period for such claim shall make payments and pay expenses, subject to applicable limits of liability, on a pro-rata basis in lieu of the non-signatory insurance policy and to the extent that such insurance policy would have had to make payments under the Agreement, up to the applicable limits of such insurance policy; provided, that the directly overlying excess insurance policy shall make such payments and pay such expenses in lieu of the non-signatory insurance policy only if no other insurance policies in the coverage block cover a part of the exposure period for such claim. Thereafter, upon a final settlement or final judicial determination described in Paragraphs 1 and 2 hereinabove, each Subscribing Insurer contributing hereunder shall, at its option, be reimbursed by the Subscribing Producer; provided, that total reimbursement of all such

contributing Insurers shall not exceed the monies received by the Producer from the non-signatory Insurer to administer, handle or dispose of asbestos-related claims plus investment income, if any, on such monies and less payments made and expenses paid directly by such Subscribing Producer for asbestos-related claims or incurred in obtaining such judicial determination or settlement agreement.

4. Whenever, with respect to an insurance policy described in Paragraph 1 hereinabove, the Subscribing Producer in question does not obtain a final settlement agreement or final judicial determination pursuant to Paragraphs 1 and 2 hereinabove within two years of the date upon which a Subscribing Insurer first has actually made liability payments and actually paid allocated expenses on a pro-rata basis in lieu of such non-signatory insurance policy pursuant to Paragraph 3 hereinabove, interest shall begin to accrue at the conclusion of such two year period on all liability payments actually made and allocated expenses actually paid by such Subscribing Insurer in lieu of the non-signatory insurance policy, and shall continue until the earlier of the date that the Subscribing Producer obtains such a final settlement agreement or final judicial determination or the date that the Subscribing Insurer in question would have exhausted its obligations to make payments or to pay expenses under the Agreement if the non-signatory Insurer in question had become a signatory hereto. Such interest shall be payable on a quarterly basis from the date of first accrual at the rate of interest announced publicly by Citibank, N.A., in New York, New York, from time to time as Citibank, N.A.'s Base Rate. When the Subscribing Producer in question obtains a final settlement agreement or final judicial determination, pursuant to Paragraphs 1 and 2 hereinabove, such Producer shall be reimbursed by the Subscribing Insurer in question for interest paid on any amounts that exceed the monies to which the Subscribing Insurer is entitled under the reimbursement provisions of Paragraph 3 hereinabove.

XXI. ADDITIONAL SIGNATORIES

1. Except as otherwise provided in Paragraph 2 hereinbelow, a Producer or Insurer may become a signatory to the Agreement subsequent to June 19, 1985, only upon application to and approval by the Board of Directors of the Facility. In determining whether such a Producer or Insurer may become a signatory hereto, the Board of Directors shall determine whether the best interests of the Facility and of the other signatories would be served thereby, in order to assure that the compromises herein and commitments of resources hereunder are duly respected, that such Producer or Insurer derives no unfair advantage with respect to the other signatories and that none of the other signatories suffers any unfair disadvantage by reason of said Producer's or Insurer's failure to become a signatory to the Agreement on June 19, 1985.

2. Notwithstanding the provisions of Paragraph 1 hereinabove, a Producer or Insurer that has pending on June 19, 1985, a petition for reorganization under Chapter 11, Title 11, of the United States Code, may become a signatory to the Agreement on or before December 31, 1986; provided that:

(A) Such Producer or Insurer conditionally subscribed to the Agreement prior to June 19, 1985;

(B) Such Producer or Insurer covenants and agrees to be bound by all of the provisions contained herein and in the Appendices hereto,

including the respective allocations of liabilities, costs and expenses pursuant to Appendices A-1 and A-2; and

(C) The court of competent jurisdiction in such Chapter 11 proceeding shall have confirmed, by December 31, 1986, a plan of reorganization authorizing and directing such Producer or Insurer to become a signatory to the Agreement or ratifying said action.

3. With respect to any Producer or Insurer that becomes a signatory hereto pursuant to Paragraph 1 or Paragraph 2 hereinabove, Sections VIII through and including XIX of the Agreement shall not apply between such Producer and each of its Subscribing Insurers or between such Insurer and each of its Subscribing Producers, as the case may be, absent the express written consent of the Subscribing Insurer or Subscribing Producer in question. In the absence of such consent, the insurance policies in question shall be treated under Section XX as if issued by an Insurer that is not a signatory hereto.

4. Each person that subsequent to June 19, 1985, pursues litigation, other than as provided for under the Agreement, against a Subscribing Producer or Subscribing Insurer concerning matters within the scope of the Agreement shall, upon becoming a signatory hereto:

(A) Reimburse each Subscribing Producer or Subscribing Insurer for all attorneys' fees and costs incurred in such litigation after June 19, 1985, and prior to the date such Producer or Insurer becomes a signatory hereto;

(B) Forgo any claims for attorneys' fees and costs incurred in such litigation after June 19, 1985, and prior to the date such Producer or Insurer becomes a signatory hereto; and,

(C) Reimburse each such Subscribing Producer or Subscribing Insurer for all damages (including punitive damages) paid by such Subscribing Producer or Subscribing Insurer as a result of such litigation.

5. The application of the Agreement provided for herein is reasonable and necessary to obtain sufficient participation in the Agreement by Producers and Insurers on or before June 19, 1985, to ensure the continued viability of the Facility and to further and protect the interests of the signatories hereto.

XXII. MODIFICATION, TERM AND CHOICE OF LAW

1. The Agreement, including Appendices A through E hereto, is the entire agreement between and among Subscribing Producers and Subscribing Insurers for the administration, defense, payment and disposition of asbestos-related claims. All antecedent or contemporaneous extrinsic representations, warranties or collateral provisions concerning the negotiation and preparation of the Agreement and the Appendices hereto are intended to be discharged and nullified. In any dispute involving the Agreement or the Appendices hereto, no signatory shall introduce evidence of or seek to compel testimony concerning any oral or written communication made prior to June 19, 1985, with respect to the negotiation and preparation of the Agreement. Any modifications to the Agreement and Appendix B hereto may be made only by mutual

agreement of all Subscribing Producers and Subscribing Insurers and in writing. Modifications to Appendices A, C, D and E may be made as provided therein.

2. All disputes concerning the validity, interpretation and application of the Agreement or the Appendices hereto, or any provision thereof, and all disputes concerning issues within the scope of the Agreement shall be determined in accordance with applicable common law of the states of the United States.

3. The Agreement shall have perpetual existence, notwithstanding the failure or invalidation of any particular provision in the Agreement or the Appendices hereto. Except as otherwise provided in the Agreement, neither termination of the Facility, termination of Facility membership nor withdrawal pursuant to Section IV hereinabove shall relieve a signatory to the Agreement of its rights and obligations hereunder, and each such signatory shall continue to abide and be bound by all of the terms and conditions of the Agreement and the Appendices hereto.

XXIII. DEFINITIONS

As used in this Agreement and the Appendices hereto, the following terms shall have the following meanings:

1. Allocated Expenses--means all fees and expenses incurred for services performed outside the Facility that can be directly attributed to the defense and disposition of a particular asbestos-related claim.

2. Asbestos-Related Claims--means any claims or lawsuits against any Subscribing Producers, Subscribing Insurers or the Facility, by whomever brought and in whatever procedural posture such claims or lawsuits may arise, seeking monetary relief (whether or not such relief is the only relief sought) for bodily injury, sickness, disease or death, alleged to have been caused in whole or in part by any asbestos or asbestos-containing product; provided, that asbestos-related claims shall not include claims for damage to or destruction of property or statutory claims for compensation by an employee against an employer.

3. Deductibles--means, with respect to any insurance policy, that part of liability payments or, if the insurance policy so provides, that part of allocated expenses to be paid directly by the policyholder or reimbursed by the policyholder to the Insurer issuing such insurance policy.

4. Insurers--means persons that are or were engaged in the business of providing liability insurance to Producers. "Primary Insurers" means Insurers that have issued primary insurance policies to Producers. "Excess Insurers" means Insurers that have issued excess insurance policies to Producers.

5. Liability Payments--means the sums paid in settlement of, or in satisfaction of a judgment on, any asbestos-related claims, exclusive of allocated and unallocated expenses for such claims.

6. Persons--means natural persons and organizations of any kind.

7. Pre-1966 Standard Form Insurance Policy--means an insurance policy containing substantially the same defense-of-suits-clause as the pre-10/1/66 National Bureau of Casualty Underwriters editions of the standard general liability insurance policy.

8. Producers--means persons that are or were engaged in the mining, manufacturing, production, processing, fabrication, distribution, installation, sale or use of asbestos or asbestos-containing products or that may have a liability with respect to asbestos-related claims.

9. Retrospective Rating Plans--means rating plans that establish premiums based in whole or in part upon the policyholder's actual loss experience under the insurance policy.

10. Self-Insured Retention--means the amount that is to be paid or assumed by the policyholder and which amount must be exceeded before overlying insurance will respond for coverage.

11. Start-Up Costs--means those costs incurred by Insurers to establish the Facility, including funds used to purchase or lease Facility assets and to hire Facility personnel.

12. Subscribing Insurers--means Insurers that have become signatories to the Agreement.

13. Subscribing Producers--means Producers that have become signatories to the Agreement.

14. Unallocated Expenses--means the overhead, operating and administrative expenses (other than allocated expenses) incurred in administering, defending and disposing of asbestos-related claims.

XXIV. SIGNATURE

The Agreement may be executed in any number of counterparts and by different signatories hereto in separate counterparts, each of which when so executed shall be deemed to be an original and all of which taken together shall constitute one and the same agreement. Each Subscribing Producer and each Subscribing Insurer shall send one executed counterpart of the Agreement to a depository to be established and maintained by the Facility.

IN WITNESS WHEREOF, the person named below has caused this Agreement to be signed by its authorized representative on this 19 day of June , 1985.

Name: Armstrong World Industries, Inc.

By: /s/ Joseph L. Jones

Title: President

Signed, sealed and delivered this 19 day of

June , 1985 , in the presence of

----- --

/s/ Harry H. Welling

Witness to the signature of the above-named person.

APPENDIX A-1

PRODUCER ALLOCATION FORMULAE

In accordance with Section VI of the Agreement, the liability payments (exclusive of punitive damage judgments) and allocated expenses incurred by the Facility on each asbestos-related claim shall be allocated among all Subscribing Producers pursuant to the formulae set forth below. Each Subscribing Producer's percentages determined in accordance with such formulae or Section H below shall be its "Allocation Percentages." The formulae apply only to Subscribing Producers who had active claims pending in the tort system as of September 30, 1983. The initial allocation percentages of "new entrants" shall be determined in accordance with Section H below.

A. LIABILITY PAYMENTS

For open claims as of September 30, 1983, plus new claims reported to Subscribing Producers or the Facility for the period October 1, 1983, to one year after the opening date of the Facility, the allocation formula is as follows:

1. For each major state: Pennsylvania, California, Texas, Washington, Massachusetts, Maryland, Virginia, New Jersey, Mississippi and Connecticut.

- (a) Determine the number of closed claims for each Producer as of September 30, 1983.
- (b) Determine the amount of indemnity dollars, including punitive damages, if any, paid or owing for each Producer as of September 30, 1983.
- (c) Divide each Producer's number of closed claims into its amount of indemnity paid or owing to arrive at an average cost per claim for each Producer.
- (d) Determine the number of open claims for each Producer as of September 30, 1983.
- (e) Multiply each Producer's number of open claims by each Producer's average cost per claim. This calculates each Producer's average cost times open claims.

2. For the remaining states the following procedure will be followed for each Subscribing Producer.

- (a) Add together the number of closed claims in all remaining states as of September 30, 1983.
- (b) Add together the amount of indemnity paid or owing, including punitive damages, if any, in all remaining states as of September 30, 1983.
- (c) Divide each Producer's total number of closed claims into each Producer's total amount of indemnity paid or owing to

arrive at each Producer's average cost per claim for states other than the major ones.

(d) Add together the number of open claims in the remaining states as of September 30, 1983.

(e) Multiply each Producer's number of open claims by its average cost per claim. This calculates each Producer's average cost times open claims for the remaining states.

3. Combining the major states' and remaining states' information:

(a) Add together each Producer's average cost times open claims (each Producer will have one amount for each major state and one amount for all remaining states).

(b) To determine each Producer's allocation percentage, divide each Producer's average cost times open claims by the aggregate of all Subscribing Producers' average cost times open claims. An adjustment will be made for each Producer that had 20 or fewer closed claims in a state. For that Producer, its simple arithmetic nationwide average cost per claim (total closed claim--all states--divided into the total amount of indemnity--all states) is used as that state's average cost per closed claim.

B. CREDIT

An additional adjustment shall be made for all claims settled between September 30, 1983, and the opening of the Facility. For each Subscribing Producer, the aggregated payments in this period will be compared to the amount each Producer would have paid in the Facility.

If a Producer's aggregated payments are equal to what it would have paid in the Facility, it will receive a full credit for such payments.

If a Producer's aggregated payments are less than what it would have paid in the Facility, it will receive credit for the full amount paid, and pay an additional amount, so that its total payments equal what it would have paid in the Facility.

If a Producer's aggregated payments are greater than what it would have paid in the Facility, it will receive a credit up to the amount it would have paid. The excess amount will be considered a "benefit" to all Subscribing Producers, and will be distributed to each (including the Producer making the payments) according to its respective allocation percentage.

C. ALLOCATED EXPENSES

Each Subscribing Producer's allocated expense percentage shall be calculated by dividing its number of open claims as of September 30, 1983, by the aggregate of all open claims as of September 30, 1983, for all Subscribing Producers.

D. PUNITIVE DAMAGES

Punitive damage judgments shall not be distributed among the Subscribing Producers according to the allocation percentages of this Appendix A-1, but shall be borne by the Subscribing Producer against which the judgment was rendered and its Insurers in accordance with the Agreement.

E. NO THIRD PARTY RIGHTS

Nothing in the Agreement or this Appendix A-1 shall obligate a non- defaulting Subscribing Producer to make any payment on behalf of a Subscribing Producer who is in default in its obligations to make payments to the Facility under this Agreement or under the By-laws of the Facility, whether by virtue of insolvency, bankruptcy or otherwise.

F. AUDIT

The data submitted by Producers shall be reviewed for accuracy, consistency, reasonableness and completeness. A Producer shall no longer be bound to its allocation percentage if any necessary audit adjustments adversely affect the Producer's allocation percentage by more than 10 percent. If such a shift results from the submission of incomplete or inaccurate data on the part of a Producer, that Producer shall be bound to its adjusted percentage.

G. PROSPECTIVE ADJUSTMENT

1. Irrespective of what information is collected for other purposes, the following types of information shall be obtained relating to pending and new claims as they enter the Facility:

- (a) Occupation of worker (see 3(a) below).
- (b) Duties of the worker.
- (c) Employment history (employers, dates, etc.).
- (d) Percentage of time involved in removal, repair or maintenance of asbestos-containing products.
- (e) Dates of exposure to asbestos-containing products.
- (f) States and/or cities where the claimant worked.
- (g) Specific projects on which the claimant worked.
- (h) Other as appropriate.

2. The following types of information shall be obtained from Subscribing Producers:

- (a) List of all types of asbestos-containing products.

(b) Date each Producer ceased placing such asbestos-containing products in the stream of commerce.

3. Allocation percentages shall be adjusted prospectively one year after the date of opening of the Facility, and at three-year intervals thereafter, to reflect changes, if any, from the occupational mix of claims included in the data base used to compute the then existing allocation percentage. This adjustment shall be made as follows:

(a) The total number of pending claims as of September 30, 1983, shall be divided into occupational categories. These categories shall include plantworker, construction (excluding insulator), shipyard (all trades involved in ship construction and repair), insulator and such other comparable categories as are significantly represented among the pending claims. Each occupational category shall be stated as a percentage of the whole. These constitute the "Facility Baseline Percentages."

(b) The calculation described in (a) above shall be performed for claims pending against each Subscribing Producer to develop its "Producer Baseline Percentages."

(c) Each Subscribing Producer's "Producer Baseline Percentages" shall be multiplied times its allocation percentage to determine its "Occupational Allocation Percentages."

(d) For claims filed after the data cutoff for the preceding allocation percentage calculation, the calculation described in (a) above shall be performed to determine changes, if any, in the "Facility Baseline Percentages." The increase or decrease in the percentage for each occupational category determined by subtracting the "Facility Baseline Percentages" from the newly determined percentages shall be referred to as the "Adjustment Factors."

(e) The percentages determined to be Adjustment Factors will be applied to the corresponding Occupational Allocation Percentages for each Producer to determine revised Occupational Allocation Percentages.

(f) Each Producer's revised Occupational Allocation Percentages shall be aggregated to determine each Producer's revised allocation percentage. Any shortfall or overage in the sum of the revised allocation percentages for all Subscribing Producers shall be distributed among the Subscribing Producers on the basis of the then applicable allocation percentages.

(g) In the event a new type of claim appears in significant numbers for which no Producer Baseline Percentages are appropriate, the Subscribing Producers shall determine appropriate sharing percentages for such claims. In the absence of agreement, the matter shall be decided pursuant to Paragraph 8 below.

(h) The data and percentages computed as a result of one prospective adjustment shall be used as the bases for the next.

4. The procedure described above shall be modified as follows to account for Subscribing Producers who have ceased placing asbestos-containing products in the stream of commerce:

(a) Determine the dates on which a Subscribing Producer ceased placing asbestos-containing products in the stream of commerce.

(b) Determine the percentage of all post-September 30, 1983, claims in which the claimant's first exposure to asbestos-containing products occurred subsequent to the date determined in (a) above. In determining this percentage, alleged post-date exposures resulting from the removal, repair or maintenance of asbestos-containing products shall be excluded from those claims with a first exposure after the date determined in (a).

(c) The percentage determined in (b) above shall be used as a component in calculating the Adjustment Factor for Producers impacted by (a) and (b) above, so as to reduce such Producer's allocation percentage.

5. No Subscribing Producer's allocation percentages shall change by more than 15 percent of its initial allocation percentages as a result of any one prospective adjustment, except as may be provided pursuant to Section H below. Any amount eliminated from the adjustment by application of this cap shall be distributed among other Subscribing Producers on the basis of their then applicable allocation percentages.

6. The percentage change in any Subscribing Producer's allocation percentage, including application of Paragraph 5 above, shall be applied to its allocation percentage for Allocated Expenses as well as Liability Payments.

7. All matters pertaining to the prospective adjustment shall be decided solely by the Subscribing Producers.

8. Any Subscribing Producer that believes that application of any prospective adjustment to its particular facts is inequitable, that any determination required by Subparagraphs G.3(a) or 4(a) above is incorrect, or that the calculation of any prospective adjustment has been performed inaccurately may take the matter to alternative dispute resolution within the Facility. Such Producer shall bear the burden of proof. If 51 percent of the Subscribing Producers with 51 percent of the allocation percentages (for liability or allocated expenses depending on the issue involved) so agree, application of the prospective adjustment may be changed without an alternative dispute resolution proceeding. This shall not preclude any Subscribing Producer who does not agree from taking the matter to alternative dispute resolution within the Facility. Such Subscribing Producer shall bear the burden of proof. No determination through alternative dispute resolution or by the Subscribing Producers may alter the 15 percent limitation established in Paragraph 5 above.

H. NEW ENTRANTS

Those Subscribing Producers whose data were not part of the data base from which the Producer allocation formulae were derived shall submit such data. In the event the data that any such Producer submits are substantially the same in qualitative and quantitative terms as the existing data base, the Producer shall have its allocation percentages computed pursuant to these formulae. Producers whose data are not substantially the same in qualitative and quantitative terms shall be admitted on a mutually-agreeable basis.

INSURER ALLOCATION OF START-UP COSTS AND OPERATING EXPENSES

1. Primary Objective

Fairness in allocation method or formula decided upon.

2. Secondary Objective

A. Ease of administration.

B. Attractiveness to prospective members, i.e., sales appeal.

C. Long-term workability.

3. Types of Funding

Funding will be divided into three main areas:

A. Funds (seed money) required to be expended before the final subscription period is concluded. These funds are reimbursable.

B. Funds provided by a single initial assessment of all Insurer subscribers to be paid no later than thirty days after the final subscription date. These funds are to be used for necessary expenses incurred before the Facility becomes operational.

C. Funds required to ensure the ongoing operation of the Facility, including the cost of the development of the data processing system and its continued operation and maintenance, including the repayment of the initial seed monies furnished by members of the Asbestos Claims Council prior to the final subscription date.

4. Method of Funding

As regards each area of funding required, a separate method is provided for:

A. First, as regards funds (seed money) required to be expended before the final subscription date or at most before a period not to exceed thirty days thereafter.

(1) It should be noted that members of the Asbestos Claims Council have already incurred many thousands of dollars of expense, and this expense is considered to be part of seed money required and will be included as part of the pre-operation expenditures as being reimbursable. It is expected that prior to the close of the final subscription period such expenses will continue to be incurred (e.g., Center for Public Resources charges, consultant fees and other similar expenses), that these expenses will continue to be paid by Council members as heretofore and that these additional expenses will likewise be reimbursable.

B. Second, as regards the single initial assessment for funds to be used for expenses between the final subscription date and the date when the Facility becomes operational:

(1) Immediately after it is determined that the number of subscriptions is sufficient so that the plan is a viable one, a nonreimbursable initial assessment fee of \$100,000 will be assessed against each and every non-Lloyds and London Company subscriber. At this same time, a nonreimbursable initial assessment fee in the amount of \$250,000 will be assessed as a total sum against all those subscribers represented by Lloyds and London Companies. All the monies collected by reason of these initial assessment fees are intended to cover expenses incurred between the end of the subscription period and the establishment of an ongoing line of credit to be established as soon as possible after the incorporation of the entity is finalized.

(2) If there should be any monies remaining in this fund when the Facility operations begin, those monies will pass into the general operating fund designed to cover the expenses of the operation.

(3) Any Insurer that subscribes to the Facility after the close of the initial subscription period will pay an initiation assessment of two times the initial assessment fee of charter subscribers, and that money will pass into the appropriate operating fund.

C. As regards funds to ensure the ongoing operation of the Facility, the cost of development, continued operation and maintenance of the data processing system and the repayment of the initial seed money to members of the Asbestos Claims Council:

(1) A surcharge which will be established by the Comptroller will be made against each Insurer (or Producer if its claims are handled by the Facility after the exhaustion of available coverage) for each of its claims as same is disposed of predicated upon (a) a percentage of indemnity paid and (b) a percentage of the allocated expenses paid. In no way or manner will the amounts of this surcharge in any way reduce or in any other manner impact the amount of indemnity coverage available to any insured.

(2) For the purposes of this surcharge, a claim will be considered to be a separate matter for each Insurer (Producer) for whom either an indemnity payment is made or an allocated expense is incurred or where both an indemnity payment is made and an allocated expense incurred for the same matter. For these purposes, the definition of indemnity payment and allocated expense is the common one used for insurance accounting purposes.

(3) The percentage of the surcharges may be different for indemnity and for allocated expense. By assessing a surcharge against indemnity, the problem which arises by reasons of Insurers (or Producers) making only indemnity payments at any one time is addressed. By assessing surcharges against allocated expense, the problem which arises by reason of the Facility successfully defending claims so that no indemnity need be paid is addressed in that these users also contribute. The underlying rationale is to assure that all users contribute to the cost of operating the Facility to the extent that the usage can be properly measured.

- (4) The amount of the surcharge will be determined after studies are concluded as to the estimation of annual likely indemnity and allocated payments.
- (5) As soon as possible after the Facility becomes a corporate entity, an initial line of credit will be obtained to ensure that sufficient funds are available for all preliminary and initial stages of the operation.
- (6) During the initial months of operation, the Comptroller will draw down from the line of credit that amount of money which is required as a difference between operating expenses and surcharges received to meet the obligations incurred by reason of organization and operating expenses.
- (7) As the Facility operations mature, there will come a time when the monthly surcharges collected will exceed the total monthly operating expenses. Those excess funds will now be applied first toward reinstating the full amount of the line of credit and thereafter toward reimbursing in equal shares those carriers who advanced seed money during the presubscription period and the time between the end of the subscription period and the collection of the assessment fees referred to in Paragraph 4-B(1).
- (8) At the time the line of credit becomes fully reimbursed, it will be reduced to an amount felt to be necessary and proper by the Comptroller to ensure against monthly shortfalls in surcharges collected.
- (9) Surcharges will continue to be levied in the same manner until the Comptroller has acquired a fund of money that will be sufficient to ensure the continued operation of the Facility for a period of at least two years forward.
- (10) At that point in time, the Comptroller will reevaluate the surcharge schedule and recommend to the Board of Directors a schedule that will continue the level of available operating funds at a level which will ensure two future years of operation.
- (11) Thereafter for the purposes of timing, an evaluation of the funding, etc. will be made twice each year e.g., as of June 30 and December 30. At that time, the Comptroller will report and make recommendations to the Board of Directors. The Board will then direct the necessary action.
- (12) The Comptroller may recommend the discontinuance of the line of credit at any time when he deems he has accumulated sufficient operating funds to ensure at least two years of future operation.
- (13) As regards the cost of development, continued operation and maintenance of the data processing system, this will be considered to be a part of the annual operating expenses of the Facility and such expenses will be covered by the surcharge in the same manner as are all other expenses.

Further, as regards the data processing system, it is contemplated:

(a) That the development costs of the system after the completion of the user specification period will be in the area of \$5,500,000. This is the best available estimate as of October, 1984.

(b) That the Facility will enter into a likely seven year contract with the vendor for the operation of the system and that the monthly charges for paying for the cost of development plus operation of the system will be in the area of \$180,000 per month. These charges will be included in the Facility operation budget.

(c) Because the payment of the development costs is spread across a contract that contemplates at least seven years of operation, it is agreed and understood by all Insurer subscribers that if the Facility should cease to operate before the development costs are fully paid, the remaining sum due will be divided among all Insurer subscribers, with the exception of Lloyds and the London companies, in equal shares in order to discharge this obligation.

APPENDIX B

CONDITIONS, DEFENSES AND EXCLUSIONS RESERVED BY SUBSCRIBING INSURERS

Subscribing Insurers reserve the right to raise only the following conditions, defenses or exclusions pursuant to Paragraph 5 of Section VIII of the Agreement, and Subscribing Producers reserve the right to contest same; disputes concerning such matters shall be resolved pursuant to Paragraph 6 of Section VIII of the Agreement:

1. That particular insurance policies were never issued or were canceled; provided, that a Subscribing Insurer that disputes the existence of an applicable insurance policy or part thereof notifies the affected Subscribing Producer of its intention to assert such a defense. The notice required under this provision shall identify the policy or policies involved and shall be given within 30 days of March 29, 1985, or of the date that the insurance policy in question is listed in the Producer's Schedules of Insurance provided to such Insurer, whichever occurs later.

2. That, with respect solely to matters occurring subsequent to June 19, 1985:

(a) the Subscribing Producer misrepresented or failed to disclose information material to an underwriter's issuance of an insurance policy, including information on the declarations page; or

(b) the Subscribing Producer breached its duties under an insurance policy, in the event of an occurrence, claim or suit, to give notice and to assist and cooperate; provided, that notice to and cooperation with the Facility shall be deemed to satisfy these duties.

3. That, with respect solely to matters occurring subsequent to June 19, 1985, or matters that were the subject of a dispute between an

Insurer and Producer prior to May 1, 1984, the Subscribing Producer failed to pay insurance policy premiums.

4. That insurance coverage is not available due to or is affected by multiple insurance policies issued solely to comply with state requirements, the inapplicability of a pre-merger or pre-acquisition insurance policy to after-acquired liabilities, exhaustion of applicable limits of liability, or the existence or non-existence of a defense obligation in an insurance policy or the obligation to provide supplementary defense payments; provided, that nothing contained herein shall be deemed to modify Sections XI, XII or XVII of the Agreement.
5. That the Subscribing Producer failed to permit inspection and audit for retrospective premium purposes for a period of three (3) years after the ending date of the insurance policy period.
6. That, subsequent to May 1, 1984, and other than by operation of the Agreement, a Subscribing Producer prejudiced the subrogation rights of a Subscribing Insurer or assigned an interest in an insurance policy without the approval of the Insurer.
7. That coverage under an insurance policy is not available due to express exclusions for claims otherwise recoverable under automobile insurance, claims for statutory worker's compensation benefits or claims otherwise recoverable under worker's compensation or employer's liability insurance.
8. That coverage under an insurance policy is not available due to express exclusions for claims involving particular territories, particular operations of the insured, particular locations, particular products or particular diseases.
9. That any changes in any insurance policies must have been made in writing pursuant to policy terms in order to be effective.
10. That the insurance policy in question does not cover punitive damage awards due to an express exclusion or because the law of the state governing the insurability of punitive damages in the particular case holds that punitive damage awards are not covered by insurance because of public policy or contract interpretation; provided, that if such holding is by other than the highest court of the state in question, the Subscribing Producer and the Subscribing Insurer each shall pay 50 percent of the punitive damage award. Any disagreement as to whether punitive damage awards are covered by insurance shall be resolved by negotiation, followed by non-binding alternative dispute resolution, followed, if necessary, by litigation. Any such resolution shall apply, in all respects, to the affected parties notwithstanding any other provision of the Agreement.

APPENDIX C

ALTERNATIVE DISPUTE RESOLUTION

INTRODUCTION

Alternative Dispute Resolution ("ADR") is the method for resolving disputed issues as provided in the Agreement. ADR involves three basic stages: 1) good-faith negotiation; 2) a proceeding concluding with a binding decision if litigation is not allowed and a non-binding decision if litigation is allowed (the "Proceeding"); and 3) an appellate process for the binding decision.

At the negotiation stage, a person (the "Neutral") will be selected who will be empowered to employ a full range of informal, mediational techniques with Principals present. After the Proceeding there will be a final settlement conference with the Judge and/or the Neutral as a last attempt to reach a Party- fashioned solution. This is to be followed by a binding decision or litigation if litigation is allowed. The binding decision may be appealed to a panel of three Judges.

Before and during formal initiation of the ADR Procedure, all Parties are strongly encouraged to engage freely in any informal negotiation desired with the express goal of reaching a negotiated solution.

OBJECTIVES

1. TO ENCOURAGE A NEGOTIATED RESULT RATHER THAN USE OF ADR.
2. TO MAXIMIZE OPTIONS FOR PRAGMATIC SOLUTIONS.
3. TO BE COST-EFFECTIVE.
4. TO BE SPEEDY.
5. TO BE EFFICIENT.
6. TO BE FAIR.
7. TO ENCOURAGE CONSISTENCY OF INTERPRETATION.

DEFINITIONS

1. Days--Business days.
2. Party--When there are more than two Parties involved in a dispute, the use of the word Party in this document shall be interpreted to mean all Parties on a side. Thus, for example, joint Parties must exercise strikes collectively.
3. Principal--An individual with settling authority for a Subscriber.
4. Subscribers--Subscribing Producers and Subscribing Insurers.

THE NEGOTIATION

Day

1.00 Negotiation Procedure

- | | | |
|---|-----|--|
| 1 | 1.1 | A Party or Parties notify the ADR branch of the Asbestos Claims Facility* ("Facility") of the dispute and request ADR. |
| 2 | 1.2 | Case is docketed by the Facility. |

2.00 Aggregation of Issues Between Disputing Parties

2.1 Issues may be aggregated only by agreement of all Parties.

3.00 Good Faith Negotiation

- | | | |
|-----------------|-----|--|
| 3 | 3.1 | The Facility shall maintain a Panel of Neutrals who have been approved by the Initial Subscribers. These Neutrals will be qualified and prepared to apply the full range of informal mediational processes and techniques. Criteria for selecting a Panel of Neutrals are set forth in Exhibit 1 hereto. |
| 5 | 3.2 | If the Parties can agree on one or more Neutrals selected from the Panel, they will notify the Facility of the name or names selected. If the Parties cannot agree, the Facility will notify the Parties of a list of seven available Neutrals. |
| 7 | 3.3 | The Parties will notify the Facility of three mutually acceptable Neutrals. Each Party may strike two names from the list provided by the Facility; the initiating Party strikes first by telephone. |
| 9 to completion | 3.4 | The Facility will notify the Parties of the name of the Neutral and the time and the place of the first meeting. There shall be no ex parte communications with the Neutral. |
| | 3.5 | Good-faith negotiations shall be held with the Principals and the Neutral present. Good-faith negotiations require that the Parties make good-faith offers and/or demands. The Parties and the Neutral should undertake to develop all options for resolution and prepare:

3.51 A statement of issues.

3.52 A statement of desired results.

3.53 An exchange of key documents, testimony, and other relevant information. |

3.54 A statement of offers.

- 3.6 If, in the judgment of the Neutral, good-faith negotiations have taken place and the Parties cannot achieve resolution, either Party may initiate the Proceeding. If the Parties feel that good-faith negotiations have taken place and the Neutral does not agree, the Parties may initiate the Proceeding. If one Party believes that good-faith negotiations have taken place, but the other Party and the Neutral disagree, the Parties shall proceed as set forth in the Procedure Manual.

* The Facility is more particularly described in Sections II through VII of the Agreement. ADR can be modified by unanimous agreement of the Parties, the Trial Judge and the Facility. The Parties may apply to the Trial Judge for modification of the ADR Procedure on a showing of good cause.

THE PROCEEDING

Day

4.00 Initiation of the Proceeding

- | | | |
|------|-----|---|
| 1 | 4.1 | The Parties notify the Facility of the request for the Proceeding. |
| 2 | 4.2 | The Facility notifies all Subscribers of the request for the Proceeding. |
| 3-10 | 4.3 | New Parties may be joined at this point if all existing Parties agree. A written consent by all Parties to such joinder must be filed with the Facility no later than seven days after notification by the Facility of the Proceeding. |
| | 4.4 | The Facility shall maintain a Panel of Trial Judges who have been approved by the Initial Subscribers. Criteria for selecting a Panel of Trial Judges are set forth in Exhibit 2 hereto. |
| 11 | 4.5 | If the Parties can agree on one or more Trial Judges from the Panel, they will notify the Facility of the name or names selected. If the Parties cannot agree, the Facility will notify the Parties of a List of seven available Trial Judges. The list of Trial Judges shall not include the Neutral, and there shall be no communication between the Trial Judge and the Neutral. |
| 13 | 4.6 | The Parties shall notify the Facility of three mutually acceptable Trial Judges. Each Party may strike two names from the list provided by the Facility; the initiating Party strikes first by telephone. |
| 15 | 4.7 | The Facility shall notify the parties of the name of the Trial Judge and the time and place of the first conference. There shall be no ex parte communications with the Trial Judge. |
| 16 | 4.8 | The Parties shall forward to the Trial Judge a joint statement of facts, issues, requested relief, and requests for documents not previously produced and other relevant information. |

19 5.00 Initial Conference. Principals need not be present.

5.1 The Trial Judge shall review and clarify the statement of dispute, issues, requested relief, and status of settlement; confirm the trial date, place and schedule; and rule on any disputes relating to document production.

6.00 Discovery

- 24 6.1 Production of Documents. Parties will produce all requested documents not previously produced. The Trial Judge will be present during the production.
- 29-38 6.2 Depositions.
- 6.21 No more than five days per side unless the Trial Judge rules otherwise. The Trial Judge has the discretion to rule otherwise in cases where there is a multiplicity of Parties or issues, or for good cause shown.
- 6.22 The Trial Judge will be present unless the Parties agree otherwise.
- 40 7.00 Pre-Proceeding Conference. The Principals and the Trial Judge must be present.
- 7.1 The Parties shall exchange and provide the Trial Judge (in writing) with:
- a. Lists of witnesses and summaries of direct testimony related to issues to be proven.

b. Exhibits related to issues to be proven.

C. Trial briefs.

- 7.2 The Trial Judge shall resolve issues such as authenticity, admissibility, etc.
- 47-57 8.00 Proceeding. The case shall be presented to the Trial Judge and the Principals, who are required to be present.
- 8.1 The first Party may put on its direct case for up to two days. The second Party may cross examine for up to one day. The Trial Judge may summarize the state of evidence.
- 8.2 The second Party may put on its direct case for up to two days. The first Party may cross examine for up to one day. The Trial Judge may summarize the state of evidence.
- 8.3 Each side may have up to one-half day for rebuttal.
- 8.4 Argument. The First Party may present direct argument for up to one hour. The Second Party may present rebuttal for up to one-half hour. The Second Party may present direct argument for up to one hour. The First Party may present rebuttal argument for up to one-half hour. Questioning by the Trial Judge is allowed.
- 8.5 A record of the Proceeding shall be kept.

- 8.6 The Trial Judge has the discretion to alter the length of the Proceeding in cases where there is a multiplicity of Parties or issues, or for good cause shown.

58 9.00 Final Settlement Conference

9.1 The Trial Judge shall meet with the Principals. If all the Parties agree, the Trial Judge may:

- a. Discuss the strengths and weaknesses of each Party's case;
- b. Question the Parties in an effort to conciliate; and
- c. Engage in mediation, as the Trial Judge sees fit.

- 60 10.A Non-Binding Decision, where the issue is one for which litigation is allowed.
- 10.A1 There will be no written opinion.
- 10.A2 An advisory opinion will be provided to any Party who requests it. The advisory opinion shall not be provided until two days after the Final Settlement Conference.
- 10.A3 Nothing from the ADR process is admissible in subsequent litigation.
- 10.A4 There will be a cooling off period of up to two days if the Trial Judge deems it advisable.
- 62 10.A5 A final negotiation session shall be held after the non-binding decision, with the Trial Judge and/or the original Neutral present, if all Parties agree.
- 10.A6 If settlement is not achieved at the final negotiation session, the Parties proceed to litigation.
- 72-79 10.B Binding Decision, where the issue is one for which litigation is not allowed. The Parties will have one week to file additional briefs or comments, and then the Trial Judge shall issue a written opinion and judgment within two weeks of the close of the Proceeding or the submission of additional papers, whichever is later. The opinion and judgment shall contain:
- 10.B1 Statement of relief granted.
- 10.B2 Statement of costs, expenses and fees awarded to the prevailing party. Prejudgment interest shall be awarded as provided in the Agreement and the Procedure Manual.

10.B3 Findings of Fact and Conclusions of Law shall be issued.

10.B4 Petitions for rehearing may be filed but will not affect the time for appeal

APPELLATE PROCESS

11.00 Appeal

1 11.1 No later than 10 days after the decision any Party desiring to appeal shall notify the Facility. The notice of appeal shall include a statement of the dispute, the requested relief, and the decision rendered below.

2 11.2 The Facility will docket the appeal and notify all Subscribers.

11.3 The Facility shall maintain a Panel of Appellate Judges who have been approved by the Initial Subscribers. Criteria for selecting a Panel of Appellate Judges are set forth in Exhibit 3 hereto.

3 11.4 If the Parties can agree on three or more Appellate Judges from the Panel, they will notify the Facility of the names selected. If the Parties cannot agree, the Facility will notify the Parties of a list of nine available Appellate Judges. The list of Appellate Judges shall not include the Neutral or the Trial Judge, and there shall be no communications between the Appellate Judges and either the Neutral or the Trial Judge.

4 11.5 The Parties shall notify the Facility of five mutually acceptable Judges. Each Party may strike two names from the list provided by the Facility; the initiating Party strikes first by telephone.

6 11.6 The Facility shall notify the Parties of the three Appellate Judge Panel and the date of the appellate pre-argument conference which shall be held three days later.

9 12.00 Appellate Pre-Argument Conference

12.1 The Court shall review the issues on appeal and the relief requested.

12.2 The Court shall confirm that the appeal is in good faith and, if all the Parties agree, shall conduct settlement negotiations as to the issues on appeal.

12.3 The Court shall confirm the appeal schedule.

- 13.00 Record On Appeal
 - 11 13.1 The Appellant shall file the record with the Facility.
 - 13 13.2 The Appellee shall supplement the record if necessary.
- 14.00 Briefs
 - 21 14.1 The Appellant's brief is due 10 days after the filing of the record.
 - 41 14.2 The Appellee's brief is due 20 days after filing of the Appellant's brief.
 - 46 14.3 The Appellant's reply brief is due five days after filing of the Appellee's brief.
- 51 15.00 Argument
 - 15.1 Appellant--45 Minutes.
 - 15.2 Appellee--One Hour.
 - 15.3 Appellant--15 Minutes.
 - 15.4 The Court may examine counsel either during the argument or after the argument is closed.
- 65 16.00 Decision. The Court shall issue a written opinion within two weeks of the close of the argument. The opinion shall contain:
 - 16.1 Statement of relief granted.
 - 16.2 Statement of costs, expenses and fees awarded to the prevailing Party. Prejudgment interest shall be awarded as provided in the Agreement and the Procedure Manual.
- 66 17.00 Rehearing. The procedure for Rehearing at the appellate level (and at the Proceeding) shall be as provided in the Procedure Manual.

100.00 Miscellaneous Provisions

100.1 Amicus Curiae Briefs

- a. Any Subscriber may file an amicus curiae brief as a matter of right at either the Proceeding or Appellate stage.
- b. The Court may accord the brief whatever weight it deems appropriate.

100.2 The standard for reversal on appellate review is whether the decision is clearly erroneous. If all

Parties request, the Trial Judge may help the Parties resolve their differences, and efforts by the Trial Judge in this regard are not subject to appeal.

100.3 All questions of law, including conflicts of law and burden of proof, shall be resolved by the Trial Judge as provided in the Procedure Manual.

100.4 The Trial Judge and the Appellate Panel shall have the power to impose sanctions for failure to comply with any aspect of the ADR Procedure. Sanctions also may be imposed for frivolous appeals and frivolous petitions for rehearing. The sanctions may include costs, fees, and expenses; the relief requested by any Party; and any further monetary or other sanctions that the Trial Judge or the Appellate Panel deems appropriate. There will be a right of appeal with regard to any award of sanctions by the Trial Judge.

100.5 The Board of Directors of the Facility shall provide guidance and instructions regarding the ADR Procedure and all problems relating thereto, with assistance from the General Counsel's office as necessary.

100.6 There will be no precedential effect of any decisions rendered in the ADR Procedure.

100.7 All decisions in the ADR Procedure shall be filed with the Facility but will be maintained by the Facility on a confidential basis and shall be available only to Subscribers.

100.8 The Federal Rules of Evidence will be applied by the Trial Judge unless modified by the Procedure Manual. Depositions and trial transcripts in prior actions automatically will be admissible, subject to whatever weight the Trial Judge determines to give such evidence.

100.9 The Facility will bear the costs of the ADR Procedure and the costs of the Neutrals until Initiation of the Proceeding (4.00). From then on, all costs will be paid by the losing Party. The procedure for payment of such costs is provided in the Procedure Manual.

PANEL OF NEUTRALS

It is anticipated that the panel of Neutrals will be drawn primarily from the CPR Judicial List. However, all Neutrals shall be approved by the Initial Subscribers.

The criteria to be used to select a Neutral are as follows:

1. Neutral and unbiased toward any of the parties or the industries involved.
2. Distinguished and respected in the business or legal communities.
3. Available on a sustained basis and on reasonably short notice.
4. Experienced in the techniques of Alternative Dispute Resolution or willing and able to learn quickly.
5. Unquestioned integrity.
6. Experienced.
7. Creative.

EXHIBIT I

PANEL OF TRIAL JUDGES

It is anticipated that the panel of Trial Judges will be drawn primarily from the CPR Judicial List. However, all Trial Judges shall be approved by the Initial Subscribers.

The criteria to be used to select a Trial Judge are as follows:

1. Neutral and unbiased toward any of the parties or the industries involved.
2. Distinguished and respected in the business or legal communities.
3. Available on a sustained basis and on reasonably short notice.
4. Unquestioned integrity.
5. Creative.
6. Judicial experience at the trial court level.
7. Exhibits judicial temperament; that is, the judge is:
 - a. Impartial;
 - b. Patient;
 - c. Courteous;
 - d. Decisive;
 - e. Fair; and
 - f. Effective.

EXHIBIT 2
PANEL OF APPELLATE JUDGES

It is anticipated that the panel of Appellate Judges will be drawn primarily from the CPR Judicial List. However, all Appellate Judges shall be approved by the Initial Subscribers.

The criteria to be used to select an Appellate Judge are as follows:

1. Neutral and unbiased toward any of the parties or the industries involved.
2. Distinguished and respected in the business or legal communities.
3. Available on a sustained basis and on reasonably short notice.
4. Unquestioned integrity.
5. Creative.
6. Judicial experience at the appellate court level.
7. Exhibits judicial temperament; that is, the judge is:
 - a. Impartial;
 - b. Patient;
 - c. Courteous;
 - d. Decisive;
 - e. Fair; and
 - f. Effective.

EXHIBIT 3

**APPENDIX D
SCHEDULES OF INSURANCE**

Following are: 1) guidelines to assist in the completion of the Schedules of Insurance pursuant to the provisions of the Agreement; 2) the forms of Schedules to be used; and 3) the form of Schedules Certification to be executed by each Subscribing Producer and its Subscribing Insurers. All policies of insurance affording general liability, products liability or premises coverage should be scheduled hereunder. Each Subscribing Producer and each of its Subscribing Insurers shall execute the Schedules Certification (in the form set forth hereinbelow) within 20 days of the date that such Producer or Insurer becomes a signatory to the Agreement, and shall note thereon any disputed issues with respect thereto. The failure by a signatory to the Agreement so to execute the Schedules Certification within such 20 day period shall be deemed an assent to and valid execution of the Schedules in question by such signatory.

1. Initial Coverage Block: Set forth the closing date of the initial coverage block. For the definition of coverage block, see Section IX of the Agreement. All insurance policies covering the period prior to the closing date should be listed on Section 1 of the form of Schedules. All insurance policies covering the period subsequent to the closing date should be listed on Section 2 of the form of Schedules.

2. Pre-Date Insurance Policies and Post-Date Insurance Policies: Set forth the date mutually agreed upon in accordance with Section XV of the Agreement. All pre-date insurance policies and all post-date insurance policies should be listed on the appropriate Sections of the form of Schedules.

3. Insurer: Specify exactly as named in the insurance policy or other evidential document of coverage.

4. Policy Period: Refer to the actual period for which the insurance policy is in effect. For policy periods of other than 12 month multiples, see Section XVIII of the Agreement.

5. Policy Type: Specify whether primary, excess or self-insured.

6. Policy Form: Enter the codes that describe the insurance policy form:

- A. Pre-1966 Standard Form Insurance Policy, as defined in Section XXIII of the Agreement.
- B. The insurance policy does not pay allocated expenses following exhaustion of aggregate limits. See Section XII of the Agreement.
- C. The insurance policy does pay allocated expenses following exhaustion of aggregate limits. See Section XII of the Agreement.
- D. The insurance policy expressly provides coverage on a specific manifestation basis.
- E. The insurance policy expressly provides coverage on a claims-made basis.
- F. The insurance policy expressly provides coverage on a first discovery basis.
- G. The insurance policy pays allocated expenses and such expenses do not apply against aggregate limits. See Section XI of the Agreement.
- H. The insurance policy pays allocated expenses and such expenses apply against aggregate limits. See Section XI of the Agreement.
- I. The insurance policy does not pay allocated expenses. See Section XI of the Agreement.

7. Per Occurrence/Accident

Limits: Refer to the limit for any one occurrence or any one accident

8. Products Aggregate: Refer to the aggregate limit applicable to products bodily injury liability coverage. Certain insurance policies may contain a combined aggregate for bodily injury, property damage and other covered perils; if so, refer to the combined limit.

With respect to insurance policies without aggregate limits, see Section XVII of the Agreement.

9. Products Aggregate

Consumption: The function of the Aggregate Consumption Summary is to track the consumption of total products liability aggregate limits by asbestos products bodily injury claims.

With respect to an insurance policy containing a deductible that explicitly provides that payment of deductibles reduces aggregate limits, see Section XV of the Agreement.

With respect to the payment of allocated expenses applying against aggregate limits, see Section XI of the Agreement.

10. Non-Products Coverage:

To impute aggregate limits for non-products coverage, see Section XVII of the Agreement.

11. Deductibles and Retentions:

Enter the codes that describe the deductible or retention:

J. Per occurrence deductible.

K. Per claim deductible.

L. Deductible reduces the aggregate limits of the insurance policy.

M. Self-insured retention.

N. Loss limit.

Where deductibles and retentions are not limited explicitly by the insurance policy language, see Section XVI of the Agreement.

Where an insurance policy containing a deductible explicitly provides that payment

of deductibles reduces aggregate limits,

see Section XV of the Agreement.

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APPENDIX D--SCHEDULES OF INSURANCE

Attaching to and forming a part of the Agreement Concerning Asbestos- Related Claims:

Subscribing Producer:*

Initial Coverage Block Ending: //

(date)

SECTION 1 (COVERAGE BLOCK):

A. Pre-Date Insurance Policies (pre-//)

Non-Products Coverage					Retention			
Policy Period	Policy No.	Insurer**	Policy Type	Policy Form	Per Occurrence/Accident Limit	B.I. or Combined Aggregate	B.I. or Combined Aggregate Consumption	B.I. or Combined Aggregate Balance

Non-Products Coverage				Retention			
Per Occurrence/Accident Limit	Aggregate	Aggregate Consumption	Aggregate Balance	Type	Amount	Stop Loss	Retro Balance

* This includes all affiliated persons (including related companies and employees, officers and directors) covered by the insurance policies listed herein. **This includes all predecessor and successor persons of each Insurer listed herein.

APPENDIX D--SCHEDULES OF INSURANCE

Attaching to and forming a part of the Agreement Concerning Asbestos- Related Claims:

Subscribing Producer:*

Initial Coverage Block Ending: //

(date)

SECTION 1 (COVERAGE BLOCK):

B. Post-Date Insurance Policies (post-//)

					Products Coverage			
Policy Period	Policy No.	Insurer**	Policy Type	Policy Form	Per Occurrence/Accident Limit	B.I. or Combined Aggregate	B.I. or Combined Aggregate Consumption	B.I. or Combined Aggregate Balance
					Retention			
Non-Products Coverage								
Per Occurrence/Accident Limit	Aggregate	Aggregate Consumption	Aggregate Balance	Type	Amount	Stop Loss	Retro	Balance

* This includes all affiliated persons (including related companies and employees, officers and directors) covered by the insurance policies listed herein. **This includes all predecessor and successor persons of each Insurer listed herein.

** This includes all predecessor and successor persons of each Insurer listed herein.

APPENDIX D--SCHEDULES OF INSURANCE

Attaching to and forming a part of the Agreement Concerning Asbestos- Related Claims:

Subscribing Producer:*

Initial Coverage Block Ending: //

(date)

SECTION 2 (NON COVERAGE BLOCK):

A. Pre-Date Insurance Policies (pre- //)

					Products Coverage			
Policy Period	Policy No.	Insurer**	Policy Type	Policy Form	Per	B.I. or Combined	B.I. or Combined	B.I. or Combined
					Occurrence/Accident Limit	Aggregate	Aggregate Consumption	Aggregate Balance
					Retention			
					Per	Aggregate	Aggregate	Aggregate
					Occurrence/Accident Limit	Consumption	Balance	Balance
					Type	Amount	Stop Loss	Retro Balance

* This includes all affiliated persons (including related companies and employees, officers and

directors) covered by the insurance policies listed herein.

**This includes all predecessor and successor persons of each Insurer listed herein.

APPENDIX D--SCHEDULES OF INSURANCE

Attaching to and forming a part of the Agreement Concerning Asbestos- Related Claims:

Subscribing Producer:*

Initial Coverage Block Ending: //

(date)

SECTION 2 (NON COVERAGE BLOCK):

B. Post-Date Insurance Policies (post- //)

					Products Coverage			
Policy Period	Policy No.	Insurer**	Policy Type	Policy Form	Per Occurrence/Accident Limit	B.I. or Combined Aggregate	B.I. or Combined Aggregate Consumption	B.I. or Combined Aggregate Balance
Non-Products Coverage					Retention			
	Per Occurrence/Accident Limit	Aggregate	Aggregate Consumption	Aggregate Balance	Type	Amount	Stop Loss	Retro Balance

* This includes all affiliated persons (including related companies and employees, officers and directors) covered by the insurance policies listed herein.

**This includes all predecessor and successor persons of each Insurer listed herein.

**APPENDIX D--SCHEDULES OF INSURANCE
CERTIFICATION**

The foregoing comprises the Schedules of all relevant policies of insurance known to the Subscribing Producer and to any of its Subscribing Insurers as of this date. Any insurance policy that subsequently becomes relevant (by discovery or otherwise) will be added to these Schedules by amendment or addendum, and it is agreed that all Subscribing Insurers are committed to cooperate with and assist the Subscribing Producer in the continuing search for policies of insurance.

These Schedules of Insurance are subject to the terms and conditions of the Agreement to which they shall be attached and form a part thereof. The undersigned acknowledge and agree that such Schedules of Insurance are in compliance with the provisions of the Agreement.

Dated:

Subscribing Producer:

Subscribing Insurers:

APPENDIX E

INSURANCE DEFENSE PROGRAM

1. Purpose:

The purpose of the Insurance Defense Program (herein called the "Defense Program" or the "Program") shall be solely to implement the provisions of Paragraph 2 of Section XII of the Agreement.

2. Definitions:

"Covered claims" means claims to which the Defense Program applies under Section 3 below.

"Base standard charge" means the standard charge for a single pre-1966 standard form insurance policy issued to a Subscribing Producer in the lowest risk category.

"Standard charge" for any calendar year means the amount designated as such in the Subscribing Insurer's Standard Charge Notice for such calendar year.

"Base surcharge" means the surcharge for a single pre-1966 standard form insurance policy issued to a Subscribing Producer in the lowest risk category.

"Surcharge" means the amount due as a surcharge under Section 7 below.

"Reserve Fund" means the amount, including all investment income thereon, held by the Administrators for the payment of defense expenses expected under the Defense Program.

"Administrators" means those holding office as such under the Defense Program.

3. Application:

The Defense Program applies only to those asbestos-related claims against Subscribing Producers that:

(a) are being administered by the Facility; and

(b) under the Agreement would have triggered an obligation to pay allocated expenses and unallocated expenses under a pre-1966 standard form insurance policy.

The Defense Program covers only the payment of allocated expenses and unallocated expenses attributable to such claims. It does not provide coverage for liability payments. The Defense Program shall not survive termination of the Facility.

4. Participation:

Each Subscribing Insurer that has issued a pre-1966 standard form insurance policy to a Subscribing Producer shall become a participant in the Defense Program and shall be bound by all of the provisions of the Program.

Each participant shall pay promptly on notice from the Administrators all standard charges and surcharges due under the Defense Program.

5. Administrators:

The Defense Program shall be administered by a Committee of Administrators, with no less than six in number, all of which shall be participants. The Committee shall include representatives of all three classes of participants, those with relatively high, moderate or low exposure to charges under the Defense Program.

The Committee will be appointed for a designated term of years by the Insurer members of the Board of Directors of the Facility. The Board will designate carriers to be members, and the carriers will designate the individual representative who will represent them. Each Administrator shall have one vote.

The Committee of Administrators shall have the full power to administer the Defense Program including power to deal with the Facility with respect to the defense of claims subject to the Defense Program and the appropriate amounts to be paid the Facility for conducting such defense and full power to determine the financing of the Defense Program including the power to determine standard charges and surcharges and to accumulate reserves.

The Committee will adopt schedules, charges and otherwise conduct their business on the basis of majority vote. If for some reason a majority decision cannot be reached, then the matter will be referred to the Insurer members of the Board of Directors for resolution. If a majority vote is not possible at that time, then the matter is referred to the Chief Financial Officer for an absolute and binding decision.

6. Mutual Sharing or Insurance Nature of the Defense Program:

The defense expenses incurred under the Defense Program shall be shared mutually by the participants in relation to:

- (a) the number of pre-1966 standard form insurance policies issued by each such participant to Subscribing Producers; and
- (b) the degree of risk each such policy presents as estimated by the Administrators.

For the purpose of implementing subdivision (b) above, the Administrators shall classify Subscribing Producers into three risk categories with the following risk relativity factors:

Risk Category	Risk Relativity
A	3
B	2
C	1

The Administrators shall assign Producers to risk categories in accordance with their respective shares of liability payments unless, by at

least a two-thirds majority, they shall determine that such a method is not appropriate to reflect the relative risk and shall adopt another method.

7. Funding:

The Administrators shall direct the Chief Financial Officer to establish a Common Reserve Fund to hold all payments made by the participants under the Defense Program. There must be no co-mingling of monies received for this purpose with any other funds, monies or assets of the Facility. The Chief Financial Officer shall keep an account for each participant showing all amounts paid by the participant, and in the event the Administrators should ever determine that the defense fund appears to be greater than needed to meet the cost of defending covered claims, then they shall direct the Chief Financial Officer to refund the excess to the participants in the ratio that the total amount paid by each bears to the total amount paid by all participants.

For each calendar year the Administrators shall estimate the amount of defense expense expected to be incurred by the Facility in defending covered claims during the calendar year plus an amount appropriate in their judgment as a reserve against contingencies. The Administrators shall then determine the base standard charge and send each participant written notice of the participant's standard charge for such calendar year.

In the event the Administrators determine that the Reserve Fund is not sufficient to meet the expected defense expenses to be incurred, the Administrators shall estimate the amount required to meet the deficit. The Administrators shall then determine the base surcharge and send each participant written notice of the participant's portion of the total surcharge.

For the first calendar year of subscription the base standard charge for each pre-1966 standard policy shall be \$400 unless the Administrators shall determine that such an amount is plainly not appropriate.

The following section gives a pro forma example that will enable each participant to estimate its approximate standard charge for the first year as soon as the number of its policies subject to the Defense Program and their Risk Categories are known.

8. Pro Forma Examples of Standard Charges and Surcharges:

The first example uses a base standard charge of \$400 and a participant with 100 pre-1966 standard form insurance policies subject to the Program, distributed as follows: 40 in Risk Category A; 35 in Risk Category B; and 25 in Risk Category C. The participants' annual standard charge is computed as follows:

Policies	Risk Category	Risk Factor	Base Charge	Standard Charge
40	A	3	\$400	\$48,000
35	B	2	\$400	\$28,000
25	C	1	\$400	\$10,000

Total standard charge for the year: \$86,000

If a surcharge were determined to be required during the course of the year, it would be applied in a like manner as with the basic standard charge. This second example demonstrates the application of a surcharge as regards a participant with the same policy and risk distribution as above:

Policies	Risk Category	Risk Factor	Base Charge	Surcharge
40	A	3	\$200	\$24,000
35	B	2	\$200	\$14,000
25	C	1	\$200	\$ 5,000

Total surcharge for affected year: \$43,000

9. Appeals and Dispute Resolution:

The Administrators shall have power to resolve all disputes among participants relating to the Defense Program and, by at least a two-thirds majority, to extend equitable relief to an individual participant if a strict application of its rules or decisions would cause the participant undue and unfair hardship.

Any participant who is aggrieved by a decision of the Board by less than a two-thirds majority may submit the matter to binding nonjudicial dispute resolution under Appendix C of the Agreement.

1993 LONG-TERM STOCK INCENTIVE PLAN

ARTICLE I - GENERAL PROVISIONS

1.1 Purposes

The purposes of the 1993 Long-Term Stock Incentive Plan (the "Plan") are to advance the long-term success of Armstrong World Industries, Inc. (the "Company"), and to increase shareholder value by providing the incentive of long-term stock-based rewards to officers, directors and key employees. The Plan is designed to: (1) encourage stock ownership by Participants to further align their interest in increasing the value of the Company; and (2) to assist in the attraction and retention of key employees vital to the Company's success.

1.2 Definitions

For the purpose of the Plan, the following terms shall have the meanings indicated:

- (a) "Board" means the Board of Directors of the Company.
- (b) "Change in Control" means a situation where: (1) any person acquires beneficial ownership of 28 percent or more of the then outstanding voting stock of the Company and within five years thereafter disinterested directors no longer constitute at least a majority of the Board, or (2) a business combination with an interested shareholder occurs which has not been approved by a majority of disinterested directors. The terms person, beneficial ownership, voting stock, disinterested director, business combination, and interested shareholder are defined in Article 7 of the Company's Articles of Incorporation.
- (c) "Code" means the Internal Revenue Code of 1986, as amended, including any successor law thereto.
- (d) "Company" means Armstrong World Industries, Inc. and solely for purposes of determining (i) eligibility for participation in the Plan; (ii) employment; and (iii) the establishment of performance goals, shall include any corporation, partnership, or other organization of which Armstrong owns or controls, directly or indirectly, not less than 50 percent of the total combined voting power of all classes of stock or other equity interests. For purposes of this Plan, the terms "Armstrong" and "Company" shall include any successor to Armstrong World Industries, Inc.
- (e) "Committee" means the Management Development and Compensation Committee of the Board or the full Board, as the case may be.
- (f) "Common Stock" means the Common Stock of the Company, par value \$1.00 per share.
- (g) "Disability" means total and permanent disability within the meaning of Section 22 (e) (3) of the Code.
- (h) "Dividend Equivalent" means an amount equal to the cash dividend paid on one share of Common Stock for each Performance Restricted Share granted during the Performance Period. All Dividend Equivalents will be reinvested in Performance Restricted Shares at a purchase price equal to the Fair Market Value on the dividend date.
- (i) "Employee or employment" means with respect to any Non-Employee Director (as defined herein), service on the Board.
- (j) "Fair Market Value" means the closing price of the Common Stock as reported on the New York Stock Exchange Composite Transactions reporting system on the applicable date or, if no sales were made on such date, on the next preceding date on which sales of the Common Stock were made.
- (k) "Incentive Stock Option" means a Stock Option which meets the definition under Section 422 of the Code.
- (l) "Nonstatutory Stock Option" means a Stock Option which does not meet the definition of an Incentive Stock Option.

- (m) "Participant" means any officer, director or key employee who has met the eligibility requirements set forth in Section 1.6 hereof and to whom a grant has been made and is outstanding under the Plan.
- (n) "Performance Period" means, in relation to Performance Restricted Shares, any period for which performance goals have been established.
- (o) "Performance Restricted Share" means a right granted to a Participant pursuant to Article IV.
- (p) "Restricted Stock Award" means an award of Common Stock granted to a Participant pursuant to Article V.
- (q) "Restriction Period" means (1) in relation to Performance Restricted Shares, the period of time, beginning at the end of the Performance Period, during which the Participant shall not be permitted to sell, assign, transfer, pledge, or otherwise dispose of such shares, and (2) in relation to Restricted Stock Awards, the period of time during which such shares are subject to forfeiture pursuant to the Plan.
- (r) "Retirement" means termination from employment with the Company after the Participant has attained age 55 and has completed five years of service with the Company or termination of employment under circumstances which the Committee deems equivalent to retirement.
- (s) "Stock Appreciation Right" means a right granted to a Participant pursuant to Article III to surrender to the Company all or any portion of the related Stock Option and to receive in shares of Common Stock an amount equal to the excess of the Fair Market Value over the option price on the date of such exercise.
- (t) "Stock Option" means a right, granted to a Participant pursuant to Article II, to purchase, before a specified date and at a specified price, a specified number of shares of Common Stock.
- (u) "Vesting Period" means the period of time, beginning at the end of the Performance Period, during which Performance Restricted Shares are subject to forfeiture pursuant to the Plan.

1.3 Administration

The Plan shall be administered by the Management Development and Compensation Committee of the Board which shall consist of not less than three directors of the Company; provided, however, that the Board shall administer the Plan as it relates to the terms, conditions and grant of awards to Non-Employee Directors. For purposes of the Plan, the term Committee shall refer to the Management Development and Compensation Committee of the Board or the full Board, as the case may be. A majority of the Committee shall constitute a quorum, and the acts of a majority of the members present at any meeting at which a quorum is present, or acts approved in writing by a majority of the Committee, shall be deemed the acts of the Committee. Subject to the provisions of the Plan and to directions by the Board, the Committee is authorized to interpret the Plan, to adopt administrative rules, regulations, and guidelines for the Plan, and to impose such terms, conditions, and restrictions on grants as it deems appropriate. The Committee, in its discretion, may allow certain optionees holding unexercised Incentive Stock Options to convert such options to Nonstatutory Stock Options. The Committee may, with respect to Participants who are not subject to Section 16 (b) of the Exchange Act, delegate such of its powers and authority under the Plan as it deems appropriate to designated officers or employees of the Company.

1.4 Types of Grants Under the Plan

Grants under the Plan may be in the form of any one or more of the following:

- (a) Nonstatutory Stock Options
- (b) Incentive Stock Options
- (c) Stock Appreciation Rights
- (d) Performance Restricted Shares
- (e) Restricted Stock Awards

1.5 Shares Subject to the Plan and Individual Award Limitation

(a) A maximum of 4,300,000 shares of Common Stock may be issued under the Plan provided, however, that no more than 430,000 shares may be granted in the form of Restricted Stock Awards. The total number of shares authorized is subject to adjustment as provided in Section 7.1

hereof. Shares of Common Stock issued under the Plan may be treasury shares or authorized but unissued shares. No fractional shares shall be issued under the Plan.

(b) If any Stock Option granted under the Plan expires or terminates, the underlying shares of Common Stock may again be made available for the purposes of the Plan. Any shares of Common Stock that have been granted as Restricted Stock Awards, or that have been reserved for distribution in payment for Performance Restricted Shares but are later forfeited or for any other reason are not payable under the Plan, may again be made available for the purposes of the Plan.

(c) The aggregate maximum number of shares of Common Stock that may be granted to any Participant in the form of Stock Options, Stock Appreciation Rights, Performance Restricted Shares and Restricted Stock Awards in any one calendar year is 300,000.

1.6 Eligibility and Participation

Participation in the Plan shall be limited to officers, who may also be members of the Board, other key employees of the Company and directors who are not employees of the Company ("Non-Employee Directors").

ARTICLE II - STOCK OPTIONS

2.1 Grant of Stock Options

The Committee may from time to time, subject to the provisions of the Plan, grant Stock Options to such Participants. The Committee shall determine the number of shares of Common Stock to be covered by each Stock Option and shall have the authority to grant Incentive Stock Options, Nonstatutory Stock Options, or a combination thereof. Furthermore, the Committee may grant a Stock Appreciation Right in connection with a Stock Option, as provided in Article III.

2.2 Incentive Stock Option Exercise Limitations

The aggregate Fair Market Value (determined at the time an Incentive Stock Option is granted) of the shares of Common Stock with respect to which an Incentive Stock Option is exercisable for the first time by a Participant during any calendar year (under all plans of the Company) shall not exceed \$100,000 or such other limit as may be established from time to time under the Code.

2.3 Option Documentation

Each Stock Option shall be evidenced by a written Stock Option agreement between the Company and the Participant to whom such option is granted, specifying the number of shares of Common Stock that may be acquired by its exercise and containing such terms and conditions consistent with the Plan as the Committee shall determine.

2.4 Exercise Price

The price at which each share covered by a Stock Option may be acquired shall be determined by the Committee at the time the option is granted and shall not be less than the Fair Market Value of the underlying shares of Common Stock on the day the Stock Option is granted. The exercise price will be subject to adjustment in accordance with the provisions of Section 7.1 of the Plan.

2.5 Exercise of Stock Options

(a) **Exercisability.** Stock Options shall become exercisable at such times and upon the satisfaction of such conditions and in such installments as the Committee may provide at the time of grant.

(b) **Option Period.** For each Stock Option granted, the Committee shall specify the period during which the Stock Option may be exercised, provided that no Stock Option shall be exercisable after the expiration of ten years from the date the option was granted.

(c) **Exercise in the Event of Termination of Employment.**

(i) Death: Unless otherwise provided by the Committee at the time of grant, in the event of death of the Participant, the option must be exercised by the Participant's estate or beneficiaries prior to its expiration. Each option may be exercised as to all or any portion thereof regardless of whether or not fully exercisable under the terms of the grant.

(ii) Disability: Unless otherwise provided by the Committee at the time of grant, in the event of the Disability of the Participant, the option must be exercised prior to its expiration. An unexercised Incentive Stock Option will cease to be treated as such and will become a Nonstatutory Stock Option twelve months following the date of termination due to Disability. Each option may be exercised as to all or any portion thereof regardless of whether or not fully exercisable under the terms of the grant.

(iii) Retirement: Unless otherwise provided by the Committee at the time of grant, in the event of the Retirement of the Participant the option must be exercised prior to its expiration. An unexercised Incentive Stock Option will cease to be treated as such and will become a Nonstatutory Stock Option three months following the date of Retirement.

(iv) Other Terminations: Unless otherwise provided by the Committee at the time of grant, in the event a Participant ceases to be an employee of the Company for any reason other than death, Disability, or Retirement, options which are exercisable on the date of termination must be exercised within three months after termination. All options which are not exercisable on the date of termination shall be cancelled.

(v) Extension of Exercise Period: Notwithstanding all other provisions under Section 2.5(c), in the event a Participant's employment is terminated, the Committee may, in its sole discretion, extend the post termination period during which the option may be exercised, provided however that such period may not extend beyond the original option period.

(d) Exercise in the Event of Change in Control. In the event of any Change in Control, all Stock Options shall immediately become exercisable without regard to the exercise period set forth in 2.5(a).

2.6 Method of Exercise

The option may be exercised in whole or in part from time to time by written request received by the Treasurer of the Company. The option price of each share acquired pursuant to an option shall be paid in full at the time of each exercise of the option either (1) in cash, or (2) by delivering to the Company shares of Common Stock or any combination of shares and cash having an aggregate Fair Market Value equal to the option price of the shares being acquired. However, shares of Common Stock previously acquired by the Participant under the Plan or any other incentive plan of the Company shall not be utilized for purposes of payment upon the exercise of an option unless those shares have been owned by the Participant for a twelve-month period or such longer period as the Committee may determine.

ARTICLE III - STOCK APPRECIATION RIGHTS

3.1 Grant of Stock Appreciation Rights

The Committee may, in its discretion, grant Stock Appreciation Rights in connection with all or any part of an option granted under the Plan. Any Stock Appreciation Right granted in connection with an option shall be governed by the terms of the Stock Option agreement and the Plan.

3.2 Exercise of Stock Appreciation Rights

Stock Appreciation Rights shall become exercisable under the Stock Option terms set forth in Section 2.5 but shall be exercisable only when the Fair Market Value of the shares subject thereto exceeds the option price of the related option.

3.3 Method of Exercise

(a) Stock Appreciation Rights shall permit the Participant, upon exercise of such rights, to surrender the related option, or any portion thereof, and to receive, without payment to the Company (except for applicable withholding taxes), an amount equal to the excess of the Fair Market Value over the option price. Such amount shall be paid in shares of Common Stock valued at Fair Market Value on the date of exercise.

(b) Upon the exercise of a Stock Appreciation Right and surrender of the related option, or portion thereof, such option, to the extent surrendered, shall be terminated, and the shares covered by the option so surrendered shall no longer be available for purposes of the Plan.

ARTICLE IV - PERFORMANCE RESTRICTED SHARES

4.1 Grant of Performance Restricted Shares

The Committee may from time to time grant Performance Restricted Shares to Participants under which payment may be made in shares of Common Stock if the performance of the Company meets certain goals established by the Committee. Such Performance Restricted Shares shall be subject to the provisions of the Plan terms and conditions, and, if earned, a Vesting Period and a Restriction Period as the Committee shall determine.

4.2 Performance Restricted Share Agreement

Each grant of Performance Restricted Shares shall be evidenced by a written agreement between the Company and Participant to whom such shares are granted. The agreement shall specify the number of Performance Restricted Shares granted, the terms and conditions of the grant, the duration of the Performance Period, the performance goals to be achieved, and the Vesting Period and the Restriction Period applicable to shares of Common Stock earned.

4.3 Common Stock Equivalent

Each Performance Restricted Share shall be credited to an account to be maintained for each such Participant during the Performance Period and shall be deemed to be the equivalent of one share of Common Stock. At the conclusion of the Performance Period, Performance Restricted Shares earned, if any, shall be converted to shares of Common Stock subject to a Vesting Period and a Restriction Period.

4.4 Performance Goals

Performance Restricted Share awards shall be conditioned upon the Company's attainment of a specified goal with respect to one or more of the following performance measures: (i) total shareholder return; (ii) EVA as defined below; (iii) return on shareholders' equity; (iv) return on capital; (v) earnings per share; (vi) sales; (vii) earnings; (viii) cash flow; and (ix) operating income. EVA equals the dollar amount arrived at by taking net operating profit after taxes and subtracting a charge for the use of the capital needed to generate that profit. The Committee shall determine a minimum performance level below which no Performance Restricted Shares shall be payable and a performance schedule under which the number of shares earned may be less than, equal to, or greater than the number of Performance Restricted Shares granted based upon the Company's performance. The Committee may adjust the performance goals and measurements to reflect significant unforeseen events; provided, however, that the Committee may not make any such adjustment with respect to any award of Performance Restricted Shares to an individual who is then a "covered employee" as such term is defined in Regulation 1.162-27(c)(2) promulgated under Section 162(m) of the Code ("Section 162(m)"), if such adjustment would cause compensation pursuant to such Performance Restricted Share award to cease to be performance-based compensation under Section 162(m).

4.5 Performance Period

The Committee shall establish a Performance Period applicable to each grant of Performance Restricted Shares. Each such Performance Period shall commence on January 1 of the calendar year in which grants are made. There shall be no limitation on the number of Performance Periods established by the Committee, and more than one Performance Period may encompass the same calendar year. The Committee may shorten any Performance Period if it determines that unusual or unforeseen events so warrant.

4.6 Dividend Equivalents During Performance Period

During the Performance Period, a Participant shall be entitled to receive Dividend Equivalents which shall be deemed to have been reinvested in additional Performance Restricted Shares at the same time as such underlying Common Stock cash dividend is paid. Performance Restricted Shares granted through such reinvestment shall be credited to the Participant's account and shall be payable to the Participant in the same manner and at the same time as the Performance Restricted Shares with respect to which such Dividend Equivalents were issued.

4.7 Right to Payment of Performance Restricted Shares

- (a) At the conclusion of the Performance Period, the Committee shall determine the number of Performance Restricted Shares, if any, which have been earned on the basis of Company performance in relation to the established performance goals. In no event shall such number exceed 300% of the shares contingently granted.
- (b) Performance Restricted Shares earned shall be converted to shares of Common Stock and shall be represented by a stock certificate registered in the name of the Participant. Certificates evidencing such shares shall be held in custody by the Company until the restrictions thereon are no longer in effect. After the lapse or waiver of the restrictions imposed, the Company shall deliver in the Participant's name one or more stock certificates, free of restrictions, evidencing the shares of Common Stock to which the restrictions have lapsed or been waived.

4.8 Vesting Period

At the time a Performance Restricted Share grant is made, the Committee shall establish a period of time (the "Vesting Period") applicable to such shares earned, if any, which shall begin at the end of the Performance Period. During the Vesting Period, Performance Restricted Shares shall be subject to the risk of forfeiture. The Committee may provide for the lapse of such restrictions in installments and may accelerate or waive such restrictions, in whole or in part, based on service and such other factors as the Committee may determine.

4.9 Restriction Period

At the time a Performance Restricted Share grant is made, the Committee shall establish a period of time (the "Restriction Period") applicable to such shares earned, if any, which shall begin at the end of the Performance Period. During the Restriction Period, the Participant shall not be permitted to sell, assign, transfer, pledge or otherwise dispose of Performance Restricted Shares that have been earned. The Committee may provide for the lapse of such restrictions in installments, in whole or in part, based on service and such other factors as the Committee may determine.

4.10 Other Terms and Conditions

Performance Restricted Shares earned and restricted shares received with respect to such shares shall be subject to the following terms and conditions:

- (a) Except as otherwise provided in the Plan or in the Performance Restricted Share agreement, the Participant shall have all the rights of a shareholder of the Company, including the right to vote the shares.
- (b) Cash dividends paid with respect to Performance Restricted Shares shall be reinvested to purchase additional shares of Common Stock that shall be subject to the same terms, conditions, and restrictions that apply to the Performance Restricted Shares with respect to which such dividends were issued.
- (c) Except as otherwise provided in the Plan or in the Performance Restricted Share agreement, upon termination of a Participant's employment, all unvested shares subject to restriction shall be forfeited by the Participant.

4.11 Termination of Employment - Provisions During a Performance Period

- (a) In the event a Participant terminates employment during a Performance Period by reason of death, Disability, or Retirement, the Participant shall be entitled to the full number of shares earned, if any, as long as the Participant had completed a minimum of one year of employment during the Performance Period. If the termination of employment is by reason of death or Disability, all other restrictions shall lapse and shares of Common Stock shall be issued to the Participant or the Participant's designated beneficiary following the Performance Period. If the termination of employment is by reason of Retirement, any applicable Restriction Period shall continue in effect, but in no event beyond the end of the three-year period following the Participant's Retirement. Following the expiration of such Restriction Period, shares of Common Stock shall be issued to the Participant. In the event the Participant had not completed one year of employment during the Performance Period, the Participant shall forfeit all rights to earn such Performance Restricted Shares.
- (b) If a Participant terminates employment for any reason other than death, Disability, or Retirement, the Participant shall forfeit all rights to earn such Performance Restricted Shares.

(c) Notwithstanding Sections 4.11(a) and 4.11(b), in the event a Participant's employment is terminated under special circumstances, the Committee may, in its sole discretion, continue a Participant's rights to earn any or all Performance Restricted Shares and waive in whole or in part any or all remaining restrictions.

4.12 Termination of Employment - Provisions Following a Performance Period

(a) In the event a Participant terminates employment following a Performance Period by reason of death, Disability, or Retirement, all Performance Restricted Shares earned shall immediately vest. If the termination of employment is by reason of death or Disability, all other restrictions shall lapse and shares of Common Stock shall be issued to the Participant or the Participant's designated beneficiary. If the termination of employment is by reason of Retirement, any applicable Restriction Period shall continue in effect, but in no event beyond the end of the three-year period following the Participant's Retirement. Following the expiration of such Restriction Period, shares of Common Stock shall be issued to the Participant.

(b) If a Participant terminates employment for any reason other than death, Disability, or Retirement, the Participant shall forfeit all Performance Restricted Shares subject to the Vesting Period. Any applicable Restriction Period shall continue in effect, but in no event beyond the end of the three-year period following the Participant's date of termination of employment. Following the expiration of such Restriction Period, shares of Common Stock shall be issued to the Participant.

(c) Notwithstanding Sections 4.12 (a) and 4.12 (b), in the event a Participant's employment is terminated under special circumstances, the Committee may, in its sole discretion, waive in whole or in part any or all remaining restrictions.

4.13 Change in Control Provisions

In the event of any Change in Control, all Performance Restricted Shares earned shall immediately vest and restrictions shall lapse on all shares subject to restrictions as of the date of such Change in Control. Further, all Performance Restricted Shares granted, including those granted pursuant to Dividend Equivalents, shall be deemed to have been earned to the maximum extent permitted pursuant to Section 4.4 for any Performance Period not yet completed as of the effective date of such Change in Control.

ARTICLE V - RESTRICTED STOCK AWARDS

5.1 Award of Restricted Stock

The Committee may authorize awards of Common Stock to officers and key employees subject to terms, conditions, and a Restriction Period as the Committee shall determine. Restricted Stock Awards shall be used for the purposes of recruitment, recognition, and retention of key employees vital to the Company's success.

5.2 Restricted Stock Award Agreement

Each Restricted Stock Award shall be evidenced by a written agreement between the Company and the Participant to whom such award is granted. The agreement shall specify the number of shares awarded, the terms and conditions of the award, the Restriction Period, the rights of the Participant, and the consequences of forfeiture consistent with the Plan as the Committee shall determine.

5.3 Awards and Certificates

Shares of Common Stock awarded pursuant to a Restricted Stock Award shall be registered in the name of the Participant. Certificates evidencing such shares shall be held in custody by the Company until the restrictions thereon are no longer in effect. After the lapse or waiver of the restrictions imposed, the Company shall deliver in the Participant's name one or more stock certificates, free of restrictions, evidencing the shares of Common Stock to which the restrictions have lapsed or been waived.

5.4 Restriction Period

At the time a Restricted Stock Award is made, the Committee shall establish a period of time (the "Restriction Period") applicable to such award during which the shares of restricted stock are subject to the risk of forfeiture and the Participant shall not be permitted to sell, assign, transfer, pledge, or otherwise dispose of such shares. The Committee may provide for the lapse of such restrictions in installments and may accelerate or waive such restrictions, in whole or in part, based on service and such other factors as the Committee may determine.

5.5 Other Terms and Conditions

Shares of restricted stock awarded and restricted shares received with respect to such shares shall be subject to the following terms and conditions:

- (a) Except as otherwise provided in the Plan or in the Restricted Stock Award agreement, the Participant shall have all the rights of a shareholder of the Company, including the right to vote the shares.
- (b) Cash dividends paid with respect to restricted shares shall be reinvested to purchase additional shares of Common Stock that shall be subject to the same terms, conditions, and restrictions that apply to the Restricted Stock Award with respect to which such dividends were issued.
- (c) Except as otherwise provided in the Plan or in the Restricted Stock Award agreement, upon termination of a Participant's employment, all shares subject to restriction shall be forfeited by the Participant.

5.6 Termination of Employment

- (a) In the event a Participant terminates employment during the Restriction Period by reason of death or Disability, restrictions shall lapse on all shares subject to restriction at the time of such termination.
- (b) In the event a Participant terminates employment during the Restriction Period by reason of Retirement, restrictions shall lapse on a proportion of any shares subject to restriction at the time of such Retirement. Any applicable Restriction Period shall continue in effect, but in no event beyond the end of the three-year period following the Participant's Retirement. The number of shares upon which the restrictions shall lapse shall be prorated for the number of months of employment during the Restriction Period prior to the Participant's termination of employment.
- (c) If a Participant terminates employment for any reason other than death, Disability, or Retirement, the Participant shall forfeit all shares subject to restriction.
- (d) Notwithstanding Sections 5.6 (a), 5.6 (b) and 5.6 (c), in the event a Participant's employment is terminated under special circumstances, the Committee may, in its sole discretion, waive in whole or in part any or all remaining restrictions.

5.7 Change in Control Provisions

In the event of any Change in Control, restrictions shall lapse on all shares subject to restrictions as of the date of such Change in Control.

ARTICLE VI - SHARE TAX WITHHOLDING AND DEFERRAL OF PAYMENT

6.1 Share Tax Withholding

- (a) At the discretion of the Committee, share tax withholding may be included as a term of any grant of Stock Options, Stock Appreciation Rights, Performance Restricted Shares, and Restricted Stock Award.
- (b) Share tax withholding shall entitle the Participant to elect to satisfy, in whole or in part, any tax withholding obligations in connection with the issuance of shares of Common Stock earned under the Plan by requesting that the Company either:
 - (i) withhold shares of Common Stock otherwise issuable to the Participant,

or

(ii) by accepting delivery of shares of Common Stock previously owned by the Participant.

In either case, the Fair Market Value of such shares of Common Stock will generally be determined on the date of exercise for Stock Options and Stock Appreciation Rights and on the date following the Restriction Period for Performance Restricted Shares and Restricted Stock Awards. Notwithstanding the foregoing, in the case of a Participant subject to the reporting requirements of Section 16(a) of the Exchange Act, no such election shall be effective unless made in compliance with any applicable requirements of Rule 16b-3(e) or any successor Rule under the Exchange Act.

(c) Shares of Common Stock previously acquired by the Participant under the Plan or any other incentive plan of the Company shall not be utilized for satisfaction of any withholding obligation unless those shares have been owned by the Participant for a twelve-month period or such longer period as the Committee may determine.

(d) Notwithstanding any other provision hereof to the contrary, the Committee, in its sole discretion may at any time suspend, terminate, or disallow any or all entitlements to share tax withholding previously granted or extended to any Participant.

6.2 Deferral of Payment

At the discretion of the Committee, a Participant may be offered the right to defer the receipt of all or any portion of Performance Restricted Shares or Restricted Stock Awards otherwise distributable to such Participant. Such right shall be exercised by execution of a written agreement by the Participant (1), with respect to Restricted Stock Awards, prior to the expiration of the applicable Restriction Period and (2), with respect to Performance Restricted Shares, prior to the expiration of the applicable Vesting Period. Upon any such deferral, the number of shares of Common Stock subject to the deferral shall remain in the custody of the Company. Cash dividends paid with respect to these shares shall be reinvested to purchase additional shares of Common Stock that shall be subject to the same deferral provisions. All other terms and conditions of deferred payments shall be as contained in said written agreement.

ARTICLE VII - OTHER PROVISIONS

7.1 Adjustment in Number of Shares and Option Prices

Grants of Stock Options, Stock Appreciation Rights, Performance Restricted Shares, and Restricted Stock Awards shall be subject to adjustment by the Committee as to the number and price of shares of Common Stock or other considerations subject to such grants in the event of changes in the outstanding shares by reason of stock dividends, stock splits, recapitalizations, reorganizations, mergers, consolidations, combinations, exchanges, or other relevant changes in capitalization occurring after the date of grant. In the event of any such change in the outstanding shares, the aggregate number of shares available under the Plan may be appropriately adjusted by the Committee.

7.2 No Right to Employment

Nothing contained in the Plan, nor in any grant pursuant to the Plan, shall confer upon any Participant any right with respect to continuance of employment by the Company or its subsidiaries, nor interfere in any way with the right of the Company or its subsidiaries to terminate the employment or change the compensation of any employee at any time.

7.3 Nontransferability

A Participant's rights under the Plan, including the right to any shares or amounts payable, may not be assigned, pledged, or otherwise transferred except, in the event of a Participant's death, to the Participant's designated beneficiary or, in the absence of such a designation, by will or by the laws of descent and distribution; provided, however, that the Committee may, in its discretion, at the time of grant of a Nonstatutory Stock Option or by amendment of an option agreement for an Incentive Stock Option or a Nonstatutory Stock Option, provide that Stock Options granted to or held by a Participant may be transferred, in whole or in part, to one or more transferees and exercised by any such transferee, provided further that (i) any such transfer must be without consideration, (ii) each transferee must be a member of such Participant's "immediate family" or a trust established for the exclusive benefit of one or more members of the Participant's immediate family; and (iii) such transfer is specifically approved by the Committee following the receipt of a written request for approval of the transfer (no approval shall be required for Non-Employee Director transfers); and provided further that any Incentive Stock Option which is amended to permit transfers during the lifetime of the Participant shall, upon the effectiveness of such amendment, be treated thereafter as a Nonstatutory Stock Option. In the event a Stock Option is transferred as contemplated in this Section, such transfer shall become effective when approved by the Committee and such Stock

Option may not be subsequently transferred by the transferee other than by will or the laws of descent and distribution. Any transferred Stock Option shall continue to be governed by and subject to the terms and conditions of this Plan and the relevant option agreement, and the transferee shall be entitled to the same rights as the Participant as if no transfer had taken place. As used in this Section, "immediate family" shall mean, with respect to any person, any spouse, child, stepchild or grandchild, and shall include relationships arising from legal adoption.

7.4 Compliance with Government Regulations

(a) The Company shall not be required to issue or deliver shares or make payment upon any right granted under the Plan prior to complying with the requirements of any governmental authority in connection with the authorization, issuance, or sale of such shares.

(b) The Plan shall be construed and its provisions enforced and administered in accordance with the laws of the Commonwealth of Pennsylvania applicable to contracts entered into and performed entirely in such State.

7.5 Rights as a Shareholder

The recipient of any grant under the Plan shall have no rights as a shareholder with respect thereto unless and until certificates for shares of Common Stock are issued to such recipient.

7.6 Unfunded Plan

Unless otherwise determined by the Committee, the Plan shall be unfunded and shall not create (or be construed to create) a trust or separate funds. With respect to any payment not yet made to a Participant, nothing contained herein shall give any Participant any rights that are greater than those of a general creditor of the Company.

7.7 Foreign Jurisdiction

The Committee shall have the authority to adopt, amend, or terminate such arrangements, not inconsistent with the intent of the Plan, as it may deem necessary or desirable to make available tax or other benefits of the laws of foreign countries in order to promote achievement of the purposes of the Plan.

7.8 Other Compensation Plans

Nothing contained in this Plan shall prevent the Company from adopting other or additional compensation arrangements, subject to shareholder approval if such approval is required.

7.9 Termination of Employment - Certain Forfeitures

Notwithstanding any other provision of the Plan (other than provisions regarding Change in Control, including without limitation Sections 2.5, 4.13 and 5.7 which shall apply in all events) and except for Performance Restricted Shares or Restricted Stock Awards which would otherwise be free of restrictions and the receipt of which has been deferred pursuant to Section 6.2, a Participant shall have no right to exercise any Stock Option or Stock Appreciation Right or receive payment of any Performance Restricted Share or Restricted Stock Award if: (1) the Participant is discharged for willful, deliberate, or gross misconduct as determined by the Committee in its sole discretion or (2) if following the Participant's termination of employment with the Company, and within a period of three years thereafter, the Participant engages in any business or enters into any employment which the Committee in its sole discretion determines to be (a) directly or indirectly competitive with the business of the Company or (b) substantially injurious to the Company's financial interest. A Participant may request the Committee in writing to determine whether any proposed business or employment activity would justify such a forfeiture. Such a request shall fully describe the proposed activity and the Committee's determination shall be limited to the specific activity so described.

ARTICLE VIII - AMENDMENT AND TERMINATION

8.1 Amendment and Termination

The Board of Directors may modify, amend, or terminate the Plan at any time except that, to the extent then required by applicable law, rule, or regulation, approval of the holders of a majority of shares of Common Stock represented in person or by proxy at a meeting of the shareholders will be required to increase the maximum number of shares of Common Stock available for distribution under the Plan (other than increases due to adjustments in accordance with the Plan). No modification, amendment, or termination of the Plan shall adversely affect the rights of a Participant under a grant previously made to him without the consent of such Participant.

ARTICLE IX - EFFECTIVE DATE AND DURATION OF PLAN

9.1 Effective Date and Duration of Plan

The Plan shall become effective immediately upon the approval and adoption thereof at the Annual Meeting of the shareholders on April 26, 1993. All rights granted under the Plan must be granted within ten years from its adoption date by the shareholders of the Company. Any rights outstanding ten years after the adoption of the Plan may be exercised within the periods prescribed under or

pursuant to the Plan.

EXHIBIT NO. 21
(as of January 1998)

Domestic Subsidiaries -----	Jurisdiction of Incorporation -----
Armstrong Cork Finance Corporation	Delaware
Armstrong Enterprises, Inc.	Vermont
Armstrong Holdings Canada, Inc.	Delaware
Armstrong Industrial Specialties, Inc.	Pennsylvania
Armstrong Industrial Specialties International, Inc.	Nevada
Armstrong Realty Group, Inc.	Pennsylvania
Armstrong Ventures, Inc.	Delaware
Armstrong World Industries Asia, Inc.	Nevada
Armstrong World Industries (Delaware) Inc.	Delaware
Armstrong World Industries (India) Inc.	Nevada
Armstrong World Industries Latin America, Inc.	Nevada
A W I (NEVADA), INC.	Nevada
Charleswater Products, Inc.	Delaware
Chemline Industries, Inc.	Delaware
Dal-Tile International Inc. (34.4% ownership interest)	Delaware
IWF, Inc.	Nevada
I.W. Insurance Company	Vermont
The W. W. Henry Company	California
The Worthington Armstrong Venture (50%-owned unincorporated affiliate)	
Foreign Subsidiaries -----	
Alphacoustic (UK) Ltd.	England
Armstrong Acquisition Canada, Inc.	Canada
Armstrong Architectural Products S.L.	Spain
Armstrong Building Products	England
Armstrong Building Products B.V.	Netherlands
Armstrong Building Products Company (Shanghai) Ltd.	People's Republic of China
Armstrong Building Products G.m.b.H.	Germany
Armstrong Building Products S.A.	France
Armstrong Building Products S.r.l.	Italy
Armstrong Europa G.m.b.H.	Germany
Armstrong Europe Services	England
Armstrong Floor Products Europe G.m.b.H.	Germany
Armstrong Floor Products Europe Ltd.	England
Armstrong Floor Products Europe Sarl.	France
Armstrong FSC, Ltd.	Bermuda
Armstrong Hunter Douglas Limited	England
Armstrong Industrial Specialties G.m.b.H.	Germany
Armstrong Industrial Specialties International, SARL	France
Armstrong Industrial Specialties Ltd.	England
Armstrong Insulation (Panyu) Co. Ltd.	People's Republic of China
Armstrong Insulation Products	England
Armstrong Insulation Products A.G.	Switzerland
Armstrong Insulation Products Benelux, S.A.	Belgium
Armstrong Insulation Products G.m.b.H.	Germany
Armstrong Insulation Products S.A.	Spain
Armstrong Insulation Products S.A.	France
Armstrong Insulation Products Sp. zo.o.	Poland
Armstrong Insulation Products S.r.l.	Italy

Armstrong Insulation Rus.	Russia
Armstrong (Japan) K.K.	Japan
Armstrong Nova Scotia Unlimited Liability Company	Canada
Armstrong-Nylex Pty. Ltd.	Australia
Armstrong Parafon A.B.	Sweden
Armstrong (Singapore) Pte. Ltd.	Singapore
Armstrong Sweden AB	Sweden
Armstrong Textile Products G.m.b.H.	Germany
Armstrong (U.K.) Investments	England
Armstrong World Industries AB	Sweden
Armstrong World Industries Canada Ltd.	Canada
Armstrong World Industries (China) Ltd.	People's Republic of China
Armstrong World Industries de Mexico, S.A. de C.V.	Mexico
Armstrong World Industries do Brasil Ltda.	Brazil
Armstrong World Industries, G.m.b.H.	Germany
Armstrong World Industries (H.K.) Limited	Hong Kong
Armstrong World Industries Korea, Ltd.	Korea
Armstrong World Industries Ltd.	England
Armstrong World Industries Pty. Ltd.	Australia
Armstrong World Industries (Thailand) Ltd.	Thailand
Inarco Limited (40%-owned affiliate)	India
Liberty Commercial Services Ltd.	Bermuda
Novita Market SA (30%-owned affiliate)	Poland
Perfiles y Techos, S.L. (known as Peytesa)	Spain
(owned by Worthington Armstrong Espana, S.L.)	Spain
Worthington Armstrong Espana, S.L.	
Worthington Armstrong Metal Products Co. (Shanghai) Ltd.	
(owned by WAVE)	People's Republic of China
Worthington Armstrong UK	England
Worthington Armstrong Venture Europe S.A. (owned by WAVE)	France

Exhibit No. 23

Consent of Independent Auditors

The Board of Directors
Armstrong World Industries, Inc.:

We consent to incorporation by reference in Registration Statement Nos. 33-38837 and 333-6333 on Form S-3 and the Registration Statement Nos. 2-50942, 2-77936, 2-91890, 33-18996, 33-60070, 33-18998, and 33-29768 on Form S-8 of Armstrong World Industries, Inc. of our report dated February 13, 1998, relating to the consolidated balance sheets of Armstrong World Industries, Inc., and subsidiaries as of December 31, 1997 and 1996 and the related consolidated statements of earnings, cash flows and shareholders' equity and financial statement schedule for each of the years in the three-year period ended December 31, 1997, which report is included herein.

KPMG Peat Marwick LLP

Philadelphia, PA
March 19, 1998

Exhibit No. 24

POWER OF ATTORNEY

Re: 1997 Annual Report on Form 10-K -

I, James E. Marley, as a Director of Armstrong World Industries, Inc., do hereby constitute and appoint, GEORGE A. LORCH or, in the case of his absence or inability to act as such, FRANK A. RIDDICK, III, or, in the case of his absence or inability to act as such, DEBORAH K. OWEN, my agent, to sign in my name and in my behalf the Company's Annual Report on Form 10-K for the year ended December 31, 1997, and any amendments thereto, to be filed by the Company with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended, with the same effect as if such signature were made by me personally.

/s/ James E. Marley

James E. Marley

Dated February 23, 1998

(Exhibit No. 24)

All powers of attorney required to be filed are substantially identical in all material respects. Therefore, in accordance with SEC Regulation 229.601(a) Instruction 2, only the foregoing copy is being included except, however, that the manually signed copy filed with the Securities and Exchange Commission includes a complete set of powers of attorney.

All powers of attorney differ only from the form of the foregoing in that they are executed by the following parties in the capacities indicated on or about February 23, 1998, and the power by Frank A. Riddick appoints only George A. Lorch or Deborah K. Owen as his agent:

Frank A. Riddick, III	Senior Vice-President, Finance (Principal Financial Officer)
Bruce A. Leech, Jr.	Controller (Principal Accounting Officer)
H. Jesse Arnelle	Director
Van C. Campbell	Director
Donald C. Clark	Director
James E. Marley	Director
J. Phillip Samper	Director
Jerre L. Stead	Director
David W. Raisbeck	Director

I, Deborah K. Owen, Senior Vice-President and Secretary of Armstrong World Industries, Inc., a corporation organized and existing under the laws of the Commonwealth of Pennsylvania, do hereby certify that, at a meeting of the Board of Directors of said corporation duly held on the 23rd day of February, 1998, at which a quorum was present and acting throughout, the following resolutions were adopted and are now in full force and effect:

RESOLVED That the 1997 annual report on Form 10-K in the form presented to this meeting has been reviewed by the Board of Directors; and the execution thereof on behalf of the Company by George A. Lorch, Frank A. Riddick, III or Deborah K. Owen, with such changes therein and additions or deletions thereto as any of them and the legal counsel to the Company may approve, and the filing thereof with the Securities and Exchange Commission after being so executed by the requisite number of directors personally or by their respective attorneys-in-fact, are hereby authorized.

FURTHER RESOLVED That the execution of the 1997 annual report on Form 10-K by George A. Lorch, Frank A. Riddick, III and Bruce A. Leech, Jr., personally or by their respective attorneys-in-fact, as principal executive officer, principal financial officer and principal accounting officer, respectively, of the Company, is hereby authorized.

IN WITNESS WHEREOF, I have hereunto set my hand and the seal of said corporation this 5th day of March, 1998.

/s/ Deborah K. Owen

Sr. Vice President & Secretary

ARTICLE 5

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE REGISTRANT'S CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR DECEMBER 31, 1997, AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

MULTIPLIER: 1,000,000

PERIOD TYPE	12 MOS
FISCAL YEAR END	DEC 31 1997
PERIOD END	DEC 31 1997
CASH	58
SECURITIES	0
RECEIVABLES	290
ALLOWANCES	37
INVENTORY	220
CURRENT ASSETS	600
PP&E	1,976
DEPRECIATION	1,004
TOTAL ASSETS	2,376
CURRENT LIABILITIES	472
BONDS	223
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	207
OTHER SE	604
TOTAL LIABILITY AND EQUITY	2,376
SALES	2,199
TOTAL REVENUES	2,199
CGS	1,462
TOTAL COSTS	1,462
OTHER EXPENSES	413
LOSS PROVISION	0
INTEREST EXPENSE	28
INCOME PRETAX	296
INCOME TAX	111
INCOME CONTINUING	185
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	185
EPS PRIMARY	4.55
EPS DILUTED	4.50

ARTICLE 5

MULTIPLIER: 1,000,000

PERIOD TYPE	3 MOS	6 MOS	9 MOS	12 MOS
FISCAL YEAR END	DEC 31 1996	DEC 31 1996	DEC 31 1996	DEC 31 1996
PERIOD END	MAR 31 1997	JUN 30 1997	SEP 30 1997	DEC 31 1996
CASH	32	51	70	65
SECURITIES	0	0	0	0
RECEIVABLES	314	316	338	252
ALLOWANCES	33	35	41	35
INVENTORY	232	234	216	206
CURRENT ASSETS	608	626	650	565
PP&E	1,953	1,987	1,992	1,939
DEPRECIATION	985	1,019	1,031	975
TOTAL ASSETS	2,191	2,228	2,255	2,136
CURRENT LIABILITIES	376	376	394	321
BONDS	229	227	227	219
PREFERRED MANDATORY	0	0	0	214
PREFERRED	0	0	0	0
COMMON	214	214	215	0
OTHER SE	567	606	605	576
TOTAL LIABILITY AND EQUITY	2,191	2,228	2,255	2,136
SALES	518	1,096	1,671	2,156
TOTAL REVENUES	518	1,096	1,671	2,156
CGS	347	725	1,105	1,460
TOTAL COSTS	347	725	1,105	1,460
OTHER EXPENSES	97	198	317	387
LOSS PROVISION	0	0	0	46
INTEREST EXPENSE	6	14	21	23
INCOME PRETAX	68	159	228	240
INCOME TAX	23	55	90	75
INCOME CONTINUING	46	104	138	165
DISCONTINUED	0	0	0	0
EXTRAORDINARY	0	0	0	(9)
CHANGES	0	0	0	0
NET INCOME	46	104	138	156
EPS PRIMARY	1.11	2.56	3.39	3.81
EPS DILUTED	1.10	2.53	3.35	3.61

ARTICLE 5

MULTIPLIER: 1,000,000

PERIOD TYPE	3 MOS	6 MOS	9 MOS	12 MOS
FISCAL YEAR END	DEC 31 1995	DEC 31 1996	DEC 31 1995	DEC 31 1995
PERIOD END	MAR 31 1996	JUN 30 1996	SEP 30 1996	DEC 31 1995
CASH	119	83	79	257
SECURITIES	0	0	0	0
RECEIVABLES	285	291	299	247
ALLOWANCES	30	33	33	29
INVENTORY	187	197	197	196
CURRENT ASSETS	620	600	601	723
PP&E	1,885	1,921	1,938	1,854
DEPRECIATION	993	1,008	1,007	976
TOTAL ASSETS	2,077	2,066	2,116	2,150
CURRENT LIABILITIES	323	328	337	376
BONDS	188	188	215	0
PREFERRED MANDATORY	0	0	0	101
PREFERRED	244	244	0	0
COMMON	103	105	229	259
OTHER SE	419	416	548	415
TOTAL LIABILITY AND EQUITY	2,077	2,066	2,116	2,150
SALES	501	1,064	1,628	2,325
TOTAL REVENUES	501	1,064	1,628	2,325
CGS	345	709	1,094	1,581
TOTAL COSTS	345	709	1,094	2,281
OTHER EXPENSES	96	197	307	2
LOSS PROVISION	0	46	46	0
INTEREST EXPENSE	6	12	19	34
INCOME PRETAX	54	100	162	8
INCOME TAX	18	33	51	(5)
INCOME CONTINUING	36	67	111	14
DISCONTINUED	0	0	0	110
EXTRAORDINARY	0	0	(8)	0
CHANGES	0	0	0	0
NET INCOME	36	67	103	123
EPS PRIMARY	.89	1.63	2.50	2.94
EPS DILUTED	.81	1.49	2.35	2.68

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