Natuzzi United Kingdom Limited

Directors' report and financial statements

Registered number 4085911

31 December 2005

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Contents

Directors' report

The directors present their report and audited financial statements for the year ended 31 December 2005.

Principal activity and review of business

The Company acts as the holding company of La Galleria Limited and Kingdom of Leather Limited. La Galleria Limited had one retail store which sold a wide range of home furnishings. Kingdom of Leather Limited primarily sold upholstered leather furniture on a made to order basis.

In 2006 notification was received from Natuzzi S.p.A., Natuzzi United Kingdom Limited's ultimate parent undertaking, that all group financial support would be withdrawn from both La Galleria Limited and Kingdom of Leather Limited. As a result of this the directors of those companies has no option but to initiate the liquidation of the businesses. By 24th March 2006 the one La Galleria Limited retail store and eight Kingdom of Leather Limited stores had had their leases surrendered to the respective landlords and trading in them had ceased. Because of the ongoing liquidation of both La Galleria Limited and Kingdom of Leather Limited the investments shown in the balance sheets of this company have been written down to a carrying value of zero.

The Company remains reliant on funds provided to it by its ultimate parent undertaking, Natuzzi S.p.A, which has not indicated that it will cease to make funds available as needed by the Company. This should enable the Company to continue in operational existence for the foreseeable future by meeting its liabilities as they fall due for payment. As with any company placing reliance on group entities for financial support, the directors acknowledge that there can be no certainty that this support will continue although at the date of approval of these financial statements, they have no reason to believe that it will not do so.

Results and dividends

The loss for the period, after taxation amounted to £818,000 *(2004: loss of £6,709,000)*.

The directors do not recommend the payment of an ordinary dividend *(2004: £nil)*.

Directors and their interests

The directors who held office during the period and since the period end were as follows:

A Bracalello	(resigned 30 August 2005)
D C Riches	
SL Finlay	(resigned 20 July 2005)
D Tranchini	(appointed 20 July 2005)

None of the directors who held office at the end of the year had any disclosable interest in the shares of the company. Details of their interests in the ultimate parent company, Natuzzi S.p.A., are disclosed in the financial statements of that company.

According to the register of directors' interests, no rights to subscribe for shares in or debentures of the company were granted to any of the directors or their immediate families, or exercised by them, during the financial year.

Directors' report *(continued)*

Auditors

Pursuant to a shareholder's resolution, the company is not obliged to reappoint its auditors annually and KPMG LLP will therefore continue in office.

On behalf of the Board

DC Riches
Director

Riverbridge House
3065 Admirals Park
Anchor Boulevard
Crossways Business Park
Dartford
Kent
DA2 5QU

11 MAY 2006

Statement of directors' responsibilities with respect to the directors' report and the financial statements

The directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards.

The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period.

In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

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

KPMG

8 Salisbury Square
London
EC4Y 8BB
United Kingdom

Independent auditors' report to the members of Natuzzi United Kingdom Limited

We have audited the financial statements of Natuzzi United Kingdom Limited for the year ended 31 December 2005 which comprise the Profit and Loss Account, the Balance Sheet and the related notes. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities on page 3, the company's directors are responsible for the preparation of the financial statements in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Report of the independent auditors to the members of Natuzzi United Kingdom Limited *(continued)*

Going concern

In forming our opinion, we have considered the adequacy of the disclosures made in note 1 of the financial statements concerning the uncertainty as to the continuation of the support for the company by its ultimate parent undertaking. In view of the significance of this uncertainty we consider that it should be drawn to your attention but our opinion is not qualified in this respect.

Opinion

In our opinion the financial statements:

- give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2005 and of its loss for the year then ended; and
- have been properly prepared in accordance with the Companies Act 1985.

KPMG LLP

KPMG LLP
Chartered Accountants
Registered Auditor

11 May, 2006

Profit and loss account
for the year ended 31 December 2004

	Note	2005 £'000	2004 £'000
Administrative expenses		(122)	(1)
Provision for impairment of investments and intra-group debtors	8, 9	(424)	(6,708)
Operating loss		(546)	(6,709)
Interest payable and similar charges	5	(272)	-
Loss on ordinary activities	2	(818)	(6,709)
Finance cost of non-equity shares	7	-	(272)
Loss for the financial period		(818)	(6,981)

There are no recognised gains and losses other than the loss of £818,000 *(2004: loss of £6,709,000).*

A note on historical gains and losses has not been included as part of the financial statements as the results as disclosed in the profit and loss account are prepared on an unmodified historical cost basis.

All of the results arose from continuing activities.

Balance sheet
at 31 December 2005

	Note	2005 £000	2005 £000	2004 £000	2004 £000
Fixed assets					
Investments	*8*		-		-
Current assets					
Debtors	*9*	-		-	
Creditors: amounts falling due within one year	10	(4,374)		(3,828)	
Net current liabilities			(4,374)		(3,828)
Total assets less current liabilities			(4,374)		(3,828)
Creditors: amounts falling due after more than one year	*11*		(5,206)		-
Net liabilities			(9,580)		(3,828)
Capital and reserves					
Called up share capital	*12*		78		3,534
Share premium	*13*		967		1,446
Profit and loss account	*13*		(10,625)		(8,808)
Shareholders' deficit (2004: £4,934,000 non-equity shareholders funds on the FRS 4 basis)	*14*		(9,580)		(3,828)

These financial statements were approved by the board of directors on 11 MAY 2006 and were *signed on its behalf by:*

D C Riches
Director

Notes
(forming part of the financial statements)

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements, except as noted below.

In these financial statements the following new standards have been adopted for the first time:

- FRS 21 'Events after the balance sheet date';
- the presentation requirements of FRS 25 'Financial instruments: presentation and disclosure'; and
- FRS 28 'Corresponding amounts'.

The accounting policies under these new standards are set out below together with an indication of the effects of their adoption. FRS 28 'Corresponding amounts' has had no material effect as it imposes the same requirements for comparatives as hitherto required by the Companies Act 1985. FRS 21 has also had no material effect on the financial statements as it relates to disclosures only in 2005.

The corresponding amounts in these financial statements have not been required to be restated. FRS 25 permits the corresponding amounts not to be restated and the Company has adopted this approach. The financial instruments policy set out below provides further details of the 2005 and 2004 bases of accounting and of the change booked on 1 January 2005.

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules.

The company is exempt by virtue of s228 of the Companies Act 1985 from the requirement to prepare group accounts. These financial statements present information about the company as an individual undertaking and not about its group.

Under Financial Reporting Standard 1 the company is exempt from the requirement to prepare a cash flow statement on the grounds that a parent undertaking includes the company in its own published consolidated accounts.

As 100% of the company's voting rights are controlled within the group headed by Natuzzi S.p.A., a company incorporated in Italy, the company has taken advantage of the exemption contained in FRS 8 and has therefore not included disclosure of transactions or balances which form part of the group. The consolidated financial statements of Natuzzi S.p.A., within which this company is included, can be obtained from the address given in note 13.

The financial statements have been prepared on the going concern basis, notwithstanding net liabilities of 9,580,000 (*2004: net liabilities £3,828,000*) which the directors believe to be appropriate for the following reason. The company is reliant on funds provided to it by its ultimate parent undertaking, Natuzzi S.p.A which has provided the company with an undertaking that it will, for at least 12 months from the date of the approval of these financial statements, continue to make available such funds as are needed by the company. This should enable the company to continue in operational existence for the foreseeable future by meeting its liabilities as they fall due for payment. As with any company placing reliance on other group entities for financial support, the directors acknowledge that there can be no certainty that this support will continue although, at the date of approval of these financial statements, they have no reason to believe that it will not do so.

Fixed asset investments

The carrying value of investments is reviewed for impairment in periods if events or changes in circumstances indicate that the carrying value may not be recoverable.

Notes *(continued)*

Employee benefit trust

The assets and liabilities and results of the Kingdom of Leather Employee Benefit Trust have been recognised in the financial statements of the company as its own under the guidance of UITF 38, "Accounting for ESOP Trusts". On 20 September 2005 the trust was dissolved.

Taxation

The charge for taxation is based on the loss for the period and takes into account taxation deferred because of timing differences. Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

Classification of financial instruments issued by the Company

Following the adoption of FRS 25, financial instruments issued by the Company are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions:

a) they include no contractual obligations upon the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Company; and

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

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

Finance payments associated with financial liabilities are dealt with as part of interest payable and similar charges. Finance payments associated with financial instruments that are classified as part of shareholders' funds (see dividends policy), are dealt with as appropriations in the reconciliation of movements in shareholders' funds.

The Company has taken advantage of the transitional arrangements of FRS 25 not to restate corresponding amounts in accordance with the above policy. The adjustments necessary to implement this policy have been made as at 1 January 2005 with the net adjustment to net assets less minority interests, after tax, taken through the 2005 reconciliation of movements in shareholders' funds. Corresponding amounts for 2004 are presented and disclosed in accordance with the requirements of FRS 4 (as applicable in 2004). The main differences between the 2004 and 2005 bases of accounting are shown below:

Effect on the balance sheet at 1 January 2005

	£000
Shares classified as liabilities	
- falling due within more than one year	(3,935)
- accruals	(999)
Share capital	(3,456)
Share premium	(479)
Profit and loss account	(999)

The nature of the main effects upon the balance sheet at 1 January 2005 and upon the 2005 profit and loss account, statement of total recognised gains and losses and cash flow statement are as follows:

The convertible cumulative preferred ordinary shares and the cumulative redeemable preference shares are treated as part of shareholders' funds in 2004 and as liabilities in 2005, and reducing reported share capital / share premium and increasing net liabilities at the start of 2005.

Notes *(continued)*

1 Accounting policies *(continued)*

Finance payments in respect of these shares are shown in the profit and loss account after the loss for the year and are added back in the profit and loss reserve in 2004 but are charged in the profit and loss account as interest in 2005. Any cumulative unpaid finance payments in respect of these shares are now classified as liabilities and therefore increases net liabilities

The 2004 disclosures follow FRS 4 as applicable. This includes the analysis of 2004 shareholders' funds into equity and non-equity components. FRS 4 used "equity" as a sub-set of shareholders' funds, whereas FRS 25 applies the term "equity" to issued financial instruments other than those, or those components, classified as liabilities.

The effect on the current year of the new policy is firstly to present £272,000 as interest charges which would hitherto have been £272,000 of dividends.

There is no net effect on the loss for the financial period transferred to reserves.

The main effects on the primary statements in the comparative year, had FRS 25 been adopted, would have been similar to those stated above.

Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated using the contracted rate or the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account.

Dividends on shares presented within shareholders' funds

Dividends unpaid at the balance sheet date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the Company. Unpaid dividends that do not meet these criteria are disclosed in the notes to the financial statements. Dividend rights on the preferred ordinary shares are not considered to be at the discretion of the company.

2 Loss on ordinary activities before taxation

Auditors' remuneration was paid by another group company.

3 Remuneration of directors

	2005	2004
	£000	£000
Directors' emoluments	-	-

The directors' salaries were paid by another group company.

4 Staff numbers and costs

The company had no employees other than the directors during the period.

Notes *(continued)*

5 Interest payable and similar charges

	2005 £000	2004 £000
Finance costs on shares classified as liabilities	272	-

As more fully explained in the "Classification of financial instruments issued by the Company" accounting policy in note 1, classifications of payments/charges as interest payable and similar charges are determined on different bases in 2005 and 2004 due to the transitional provisions of FRS 25.

6 Taxation

Analysis of charge in period

	2005 £000	2004 £000
UK corporation tax	-	-
Tax on profit on ordinary activities	-	-

Factors affecting the tax charge for the current period

The current tax credit for the period is lower than the standard rate of corporation tax in the UK (30 %). The differences are explained below.

	2005 £000	2004 £000
Current tax reconciliation		
Loss on ordinary activities before tax	(818)	(6,709)
Current tax at 30% *(2004: 30%)*	(245)	(2,013)
Effects of:		
Expenses not deductible for tax purposes (primarily provision for impairment of investments and intra-group debtors)	215	2,013
Losses carried forward	30	-
Total current tax	-	-

Potential deferred tax assets of £30,000 (2004: £nil) related to tax losses carried forward have not been recognised in the financial statements.

7 Finance costs of non-equity shares

	2005 £000	2004 £000
8% preference shares (See notes 10 and 11)	-	268
3.907% preferred ordinary shares (See notes 10 and 11)	-	4
	-	272

The aggregate amount of finance costs recognised as liabilities as at the year end is £1,271,000 *(2004:£nil).*

As more fully explained in note 1, classifications of payments/deductions as dividends are determined on different bases in 2005 and 2004 due to the transitional provisions of FRS 25.

8 Investments

	Investment in subsidiary undertakings £000
Cost	
At 31 December 2004 and at 31 December 2005	8,668
Provision for impairment	
At 31 December 2004 and at 31 December 2005	(8,668)
Net book value	
At 31 December 2004 and at 31 December 2005	-

The companies in which Natuzzi United Kingdom Limited has an interest are as follows:

Company	**Country of incorporation**	**Class of share**	**Effective interest**	**Nature of business**
Kingdom of Leather Limited	England and Wales	Ordinary	100%	*Furniture retail
La Galleria Limited	England and Wales	Ordinary	100%	*Furniture retail

*As described in note 14, since the year end, the activities of the company's subsidiaries have been discontinued.

Notes *(continued)*

9 Debtors

	2005 £000	2004 £000
Amounts due from subsidiary undertakings	424	-
Provision	(424)	-
	-	-

10 Creditors: amounts falling due within one year

	2005 £000	2004 £000
Amounts owed to subsidiary undertakings	-	2,828
Amounts owed to parent company	4,344	1,000
Accruals	30	-
	4,374	3,828

11 Creditors: amounts falling due after one year

	2005 £000	2004 £000
Shares classified as liabilities	3,935	-
Accrued dividends	1,271	-
	5,206	-

As more fully explained in note 1, classifications of financial liabilities are determined on different bases in 2005 and 2004 due to the transitional provisions of FRS 25.

Notes *(continued)*

12 Called up share capital

	2005	2004
	£	£
Authorised		
76,655 ordinary shares of £1 each	**76,655**	76,655
108,986 3.907% convertible cumulative preferred ordinary shares of £1 each	**108,986**	108,986
3,596,774 8% cumulative redeemable preference shares of £1 each	**3,596,774**	3,596,774
2 deferred shares of £1 each	**2**	2
80,596 preferred ordinary shares of £0.01 each	**806**	806
	3,783,223	3,783,223

	2005	2004
	£000	£000
Allotted, called up and fully paid		
76,655 Ordinary shares of £1 each	**77**	77
108,986 3.907% convertible cumulative preferred ordinary shares of £1 each	**109**	109
3,346,774 8% cumulative redeemable preference shares of £1 each	**3,347**	3,347
2 deferred shares of £1 each	**-**	-
80,596 preferred ordinary shares of £0.01 each	**1**	1
	3,534	3,534
Shares classified as liabilities	**3,456**	-
Shares classified in shareholders' funds	**78**	3,534
	3,534	3,534

As more fully explained in note 1, classifications within shareholders' funds are determined on different bases in 2005 and 2004 due to the transitional provisions of FRS 25.

Convertible cumulative preferred ordinary shares

The convertible cumulative preferred ordinary shares are convertible at the option of the holders, in the event of a change of control or certain other events, into ordinary shares on the basis of one ordinary share for one convertible cumulative preferred ordinary share. They carry the right to a dividend of 3.907% per annum payable half yearly in arrears on 30 June and 31 December. The shareholders are also entitled to a variable cumulative participating dividend of 12% of the group's adjusted profits as set out in the Articles of Association in respect of each financial year of the company ending on or after 30 June 2001.

The convertible cumulative preferred ordinary shares carry one vote per share. On a winding up of the company the holders of these shares have a right to receive, in preference to ordinary shareholders, £1 per share plus any accrued dividend.

The payment of current outstanding dividends, and dividends due in June and December 2005, have been deferred until 30 June 2007.

The preferred ordinary shares of £0.01 each issued during the prior period rank pari passu with the existing preferred ordinary shares.

Notes *(continued)*

12 Called up share capital (continued)

Cumulative redeemable preference shares

The cumulative redeemable preference shares carry the right to a dividend of 8% per annum payable half yearly in arrears on 30 June and 31 December. The repayments were structured as follows:

	Number of Shares
30 June 2002	750,000
30 June 2003	750,000
30 June 2004	596,774
30 June 2005	750,000
30 June 2006	500,000

The preference share redemptions due at 30 June 2002, 2003, 2004 and 2005 have been deferred until 30 June 2007. The payment of current outstanding dividends including dividends due in June and December 2005, have also been deferred until 30 June 2007.

The cumulative redeemable preference shares are redeemable at their paid up value at the option of the company at any time. On a winding up of the company the holders of the cumulative redeemable preference shares have a right to receive, in preference to the ordinary shareholders, £1.00 per share plus any accrued dividend.

The cumulative redeemable preference shares carry no votes at meetings unless the dividends thereon or redemption thereof is six months or more in arrears, or on the occurrence of certain other events. In these events each holder will be entitled to vote for each cumulative redeemable preference share held.

No dividends can be declared or paid on the ordinary shares or further dividends on the preferred ordinary shares without the consent of the preference shareholders or until all the preference shares have been redeemed.

After the redemption of the preference shares, the ordinary shares shall have the right to receive dividends equal to the amount of the preferred dividend and participating dividend on each preferred ordinary share.

Deferred shares

The deferred shares have no right to a dividend or to participate in the profits of the company, except on a sale, winding up of the company or other return of capital where the holders of the deferred shares are entitled to £455,968.

13 Share premium and reserves

	Share premium account £000	**Profit and loss account £000**
At the beginning of the year	1,446	(8,808)
Loss for the period	-	(818)
Effect of adoption of FRS 25, net of tax, on 1 January 2005	(479)	(1,271)
At the end of the year	967	(10,625)

As more fully explained in note 1, classifications within shareholders' funds are determined on different bases in 2005 and 2004 due to the transitional provisions of FRS 25. The adjustments to share premium and reserves to reflect this new policy, and its consequential effects on the profit and loss account, are dealt with as a movement, above, in 2005.

Notes *(continued)*

14 Reconciliation of movement in shareholders' deficit

	2005 £000	2004 £000
Opening balance	(3,828)	2,915
Loss for the financial period	(818)	(6,709)
Effect of adoption of FRS 25 net of tax on 1 January 2005	(4,934)	-
Loss on sale of own shares	-	(34)
Finance cost of non-equity shares	-	(272)
Unpaid non-equity dividend	-	272
Shareholders' deficit carried forward	(9,580)	(3,828)

15 Ultimate parent company and parent undertaking of larger group of which the company is member

The immediate parent undertaking and the ultimate parent company of the company is Natuzzi S.p.A which is incorporated in Italy and listed on the NYSE.

The largest group in which the results of the company are consolidated is that headed by Natuzzi S.p.A. The consolidated financial statements of Natuzzi S.p.A are available from Natuzzi S.p.A, Via Iazzitiello 47, 70029 Santeramo in Colle (BA), Italy.

16 Events after the balance sheet date

In 2006 notification was received from Natuzzi S.p.A., Natuzzi United Kingdom Limited's ultimate parent undertaking, that all group financial support would be withdrawn from both La Galleria Limited and Kingdom of Leather Limited. As a result of this the directors of those companies has no option but to initiate the liquidation of the businesses. By 24th March 2006 the one La Galleria Limited retail store and eight Kingdom of Leather Limited stores had had their leases surrendered to the respective landlords and trading in them had ceased. Because of the ongoing liquidation of both La Galleria Limited and Kingdom of Leather Limited the investments shown in the balance sheets of this company have been written down to a carrying value of zero.