

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

FORM 10-Q

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

For the quarterly period ended July 1, 2006

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 333-124138

**SIMMONS COMPANY**

(Exact name of registrant as specified in its charter)

Delaware

20-0646221

(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer Identification No.)

One Concourse Parkway, Suite 800, Atlanta, Georgia

30328-6188

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code (770) 512-7700

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

Yes:  No:

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

Large accelerated filer:  Accelerated filer:  Non-accelerated filer:

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes:  No:

The number of shares of the registrant's common stock outstanding as of August 1, 2006: 4,448,211.36

DOCUMENTS OR PARTS THEREOF INCORPORATED BY REFERENCE: None

**PART I — FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**Simmons Company and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Operations**  
**and Comprehensive Income (Loss)**  
(In thousands)

	Quarters Ended		Six Months Ended	
	July 1, 2006	June 25, 2005	July 1, 2006	June 25, 2005
Net sales	\$ 241,202	\$ 208,042	\$ 477,069	\$ 413,624
Cost of products sold	132,051	117,256	268,490	231,422
Gross profit	<u>109,151</u>	<u>90,786</u>	<u>208,579</u>	<u>182,202</u>
Operating expenses:				
Selling, general and administrative expenses	81,633	73,342	152,539	152,503
Amortization of intangibles	1,417	1,417	2,834	2,858
Licensing revenues	(2,012)	(2,815)	(4,300)	(4,866)
	<u>81,038</u>	<u>71,944</u>	<u>151,073</u>	<u>150,495</u>
Operating income	28,113	18,842	57,506	31,707
Interest expense, net	<u>24,715</u>	<u>17,359</u>	<u>43,891</u>	<u>33,773</u>
Income (loss) before income taxes	3,398	1,483	13,615	(2,066)
Income tax expense (benefit)	<u>1,337</u>	<u>424</u>	<u>5,121</u>	<u>(933)</u>
Net income (loss)	2,061	1,059	8,494	(1,133)
Other comprehensive income (loss):				
Foreign currency translation adjustment	71	(9)	115	(6)
Comprehensive income (loss)	<u>\$ 2,132</u>	<u>\$ 1,050</u>	<u>\$ 8,609</u>	<u>\$ (1,139)</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

**Simmons Company and Subsidiaries**  
**Condensed Consolidated Balance Sheets**  
(Dollars in thousands)

	July 1, 2006	December 31, 2005*
	(Unaudited)	
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 28,882	\$ 24,622
Accounts receivable, less allowances for doubtful receivables, discounts and returns of \$4,900 and \$4,032	88,494	76,032
Inventories	28,842	33,050
Deferred income taxes	2,931	2,865
Other current assets	15,767	15,085
<b>Total current assets</b>	<b>164,916</b>	<b>151,654</b>
Property, plant and equipment, net	59,075	58,360
Goodwill	488,185	488,230
Intangible assets, net	534,456	537,290
Other assets	35,592	45,243
	<b>\$ 1,282,224</b>	<b>\$ 1,280,777</b>

\* Derived from the Company's 2005 audited consolidated financial statements.

The accompanying notes are an integral part of these condensed consolidated financial statements.

**Simmons Company and Subsidiaries**  
**Condensed Consolidated Balance Sheets**  
(Dollars in thousands)

	July 1, 2006	December 31, 2005*
	(Unaudited)	
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current liabilities:</b>		
Current maturities of long-term debt	\$ 413	\$ 1,602
Accounts payable	52,397	45,031
Accrued liabilities	66,323	65,139
<b>Total current liabilities</b>	<b>119,133</b>	<b>111,772</b>
<b>Non-current liabilities:</b>		
Long-term debt	886,444	906,148
Deferred income taxes	148,861	144,418
Other	14,641	14,092
<b>Total liabilities</b>	<b>1,169,079</b>	<b>1,176,430</b>
<b>Commitments and contingencies</b>		
<b>Stockholders' equity:</b>		
Class A common stock, \$.01 par value: Authorized - 4,000,000 shares issued and outstanding - 3,878,307 shares	39	39
Class B common stock, \$.01 par value: Authorized, issued and outstanding - 688,235 shares	7	7
Additional paid-in capital	102,486	102,337
Retained earnings	13,037	4,648
Accumulated other comprehensive income	249	134
Deferred compensation	-	(361)
Treasury stock, at cost, 60,118 and 46,860 shares of class A common stock and 58,213 and 48,411 shares of class B common stock	(2,673)	(2,457)
<b>Total stockholders' equity</b>	<b>113,145</b>	<b>104,347</b>
	<b>\$ 1,282,224</b>	<b>\$ 1,280,777</b>

\* Derived from the Company's 2005 audited consolidated financial statements.

The accompanying notes are an integral part of these condensed consolidated financial statements.

**Simmons Company and Subsidiaries**  
**Unaudited Condensed Consolidated Statements of Cash Flows**  
(In thousands)

	Six Months Ended	
	July 1, 2006	June 25, 2005
<b>Cash flows from operating activities:</b>		
Net income (loss)	\$ 8,494	\$ (1,133)
<b>Adjustments to reconcile net income (loss) to net cash provided by operating activities:</b>		
Depreciation and amortization	14,057	13,121
Provision for bad debts, net	868	(107)
Provision for deferred income taxes	4,528	(1,363)
Non-cash interest expense	16,629	9,457
Non-cash stock compensation expense	517	-
<b>Net changes in operating assets and liabilities:</b>		
Accounts receivable	(13,330)	13,625
Inventories	4,209	818
Other current assets	(682)	2,311
Accounts payable	7,366	(2,728)
Accrued liabilities	1,058	(12,835)
Other, net	(2,470)	(2,820)
Net cash provided by operating activities	<u>41,244</u>	<u>18,346</u>
<b>Cash flows from investing activities:</b>		
Purchases of property, plant and equipment	(5,776)	(2,586)
Purchase of certain assets of Simmons Juvenile Products, Inc.	-	(3,337)
Net cash used in investing activities	<u>(5,776)</u>	<u>(5,923)</u>
<b>Cash flows from financing activities:</b>		
Borrowings under New Senior Credit Facility, net	480,000	-
Payments of senior credit facility, net	(369,933)	(4,668)
Repayment of senior unsecured term loan	(140,000)	-
Payments of other debt	(106)	(158)
Payments of financing fees	(973)	(125)
Purchase of treasury stock	(311)	(304)
Net cash used in financing activities	<u>(31,323)</u>	<u>(5,255)</u>
Net effect of exchange rate changes on cash	115	(6)
Change in cash and cash equivalents	4,260	7,162
Cash and cash equivalents, beginning of period	24,622	24,206
Cash and cash equivalents, end of period	<u>\$ 28,882</u>	<u>\$ 31,368</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

**Simmons Company and Subsidiaries**  
**Condensed Consolidated Statement of Changes in Stockholders' Equity**  
(Dollars in thousands)

	Class A		Class B		Additional Paid-In Capital	Retained Earnings	Accumulated	Deferred Compensation	Common	Total Stockholders' Equity
	Common	Common	Common	Common			Other		Stock	
	Shares	Stock	Shares	Stock			Income		Held In Treasury	
<b>December 31, 2005 (audited)</b>	3,831,447	\$ 39	639,824	\$ 7	\$ 102,337	\$ 4,648	\$ 134	\$ (361)	\$ (2,457)	\$ 104,347
Net income	-	-	-	-	-	8,494	-	-	-	8,494
Other comprehensive income:										
Change in foreign currency translation	-	-	-	-	-	-	115	-	-	115
Comprehensive income						8,494	115	-	-	8,609
Issuance of Class B common stock held in treasury	-	-	84,850	-	12	(105)	-	-	95	2
Non-cash stock compensation expense	-	-	-	-	517	-	-	-	-	517
Adoption of Statement of Financial Standards 123R	-	-	-	-	(361)	-	-	361	-	-
Tax shortfall resulting from restricted stock awards	-	-	-	-	(19)	-	-	-	-	(19)
Purchase of treasury stock, at cost	(13,258)	-	(94,652)	-	-	-	-	-	(311)	(311)
<b>July 1, 2006 (unaudited)</b>	<u>3,818,189</u>	<u>\$ 39</u>	<u>630,022</u>	<u>\$ 7</u>	<u>\$ 102,486</u>	<u>\$ 13,037</u>	<u>\$ 249</u>	<u>\$ -</u>	<u>\$ (2,673)</u>	<u>\$ 113,145</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

**Simmons Company and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**

**A. Basis of Presentation**

Simmons Company is a holding company with no operating assets. Through its wholly-owned subsidiary THL-SC Bedding Company, which is also a holding company, Simmons Company owns the common stock of Simmons Bedding Company. All of Simmons Company's business operations are conducted by Simmons Bedding Company and its direct and indirect subsidiaries (collectively "Simmons Bedding"). Simmons Company, together with its subsidiaries (collectively the "Company" or "Simmons Company"), is one of the largest bedding manufacturers in the United States.

These condensed consolidated financial statements of the Company are unaudited, and have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and the rules and regulations of the Securities and Exchange Commission (the "Commission"). The accompanying unaudited condensed consolidated financial statements contain all adjustments, which, in the opinion of management, are necessary to present fairly the financial position of the Company as of July 1, 2006, and its results of operations and cash flows for the periods presented herein. All adjustments in the periods presented herein are normal and recurring in nature unless otherwise disclosed. These unaudited condensed consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2005. Operating results for the periods ended July 1, 2006 are not necessarily indicative of future results that may be expected for the fiscal year ending December 30, 2006 or for any future period.

The preparation of unaudited condensed consolidated financial statements in conformity with GAAP includes some amounts that are based upon management estimates and judgments. Future actual results could differ from such current estimates.

**B. Inventories**

A summary of inventories follows (in thousands):

	<b>July 1, 2006</b>	<b>December 31, 2005</b>
Raw materials	\$ 14,120	\$ 18,541
Work-in-progress	779	1,261
Finished goods	9,164	8,777
Inventory held at retail stores	4,779	4,471
	<u>\$ 28,842</u>	<u>\$ 33,050</u>

### C. Goodwill

The changes in the carrying amount of goodwill for the six months ended July 1, 2006 are as follows (in thousands):

	<b>Wholesale Bedding</b>	<b>Retail</b>	<b>Consolidated</b>
Balance as of December 31, 2005	\$ 481,279	\$ 6,951	\$ 488,230
Tax benefit allocated to reduce goodwill	(45)	-	(45)
Balance as of July 1, 2006	<u>\$ 481,234</u>	<u>\$ 6,951</u>	<u>\$ 488,185</u>

### D. Warranties

The conventional bedding products that the Company currently manufactures generally include a ten year non-prorated warranty. The Company's warranty accrual is an estimate of future warranty returns recorded at the current average cost to settle warranty claims. The accrual is calculated as follows:

- 1) The Company records the amount of warranties issued during the period based upon its units sold, the cumulative average return rate for the previous ten years, and the estimated average cost to settle a warranty claim.
- 2) The Company adjusts the accruals related to pre-existing warranties for the estimated average cost to settle a warranty claim and changes in its estimate of the number of future warranty returns resulting from changes in its cumulative average return rate for the previous ten years.
- 3) The Company reduces the accrual for warranty settlements during the period based upon the number of warranty returns recorded at the estimated cost to settle warranty claims. The estimated cost to settle a warranty claims is based upon the average manufacturing cost per unit, including freight, less anticipated cost recovery resulting from the selling of returned product to "as-is" dealers and to consumers through the Company's owned retail outlet stores.

The following table presents a reconciliation of the Company's warranty accrual for the periods ended July 1, 2006 and June 25, 2005 (in thousands):

	Quarters Ended		Six Months Ended	
	July 1, 2006	June 25, 2005	July 1, 2006	June 25, 2005
Balance at beginning of period	\$ 3,091	\$ 2,858	\$ 3,009	\$ 2,715
Additional warranties issued	429	502	1,054	1,014
Warranty settlements	(441)	(193)	(884)	(950)
Revisions of estimate	(136)	(52)	(236)	336
Balance at end of period	\$ 2,943	\$ 3,115	\$ 2,943	\$ 3,115

As a result of a decrease in warranty returns combined with a lower cost to settle warranty claims, our warranty accrual as of July 1, 2006 was \$0.2 million less than the accrual as of June 25, 2005.

#### E. Long-Term Debt

A summary of long-term debt follows (in thousands):

	July 1, 2006	December 31, 2005
Senior credit facility:		
Revolving loan	\$ -	\$ -
Tranche C term loan	-	369,933
Tranche D term loan	480,000	-
Total senior credit facility	480,000	369,933
Senior unsecured term loan	-	140,000
7.875% senior subordinated notes due 2014	200,000	200,000
10.0% senior discount notes, due 2014, net of discount of \$77,025 and \$86,172	191,975	182,828
Other, including capital lease obligations	14,882	14,989
	886,857	907,750
Less current portion	(413)	(1,602)
	\$ 886,444	\$ 906,148

On May 25, 2006, Simmons Bedding executed the second amended and restated senior credit and guaranty agreement ("New Senior Credit Facility") with a syndicate of lenders, which amends and restates its existing senior credit facility in its entirety. The New Senior Credit Facility provides for a \$75.0 million revolving credit facility and a \$492.0 million tranche D term loan facility. The proceeds from the New Senior Credit Facility were used to replace Simmons Bedding's \$350.0 million tranche C term loan and \$140.0 million senior unsecured term loan. This exchange of debt instruments is referred to as the "Refinancing". Among other things, the New Senior Credit Facility reduces the applicable Eurodollar and Base interest rate margins for borrowings under the term loan.

In connection with the Refinancing, Simmons Bedding paid approximately \$1.9 million in call premiums, agency fees and legal fees (collectively, the "Refinancing Costs"). The Refinancing Costs were recorded in accordance with Emerging Issues Task Force 96-19, *Modification of Debt Instruments with Different Terms* ("EITF 96-19"). Under EITF 96-19, Simmons Bedding compared each syndicated lenders' loan under the tranche D term loan with the syndicated lenders' loan under the tranche C term loan and senior unsecured term loan. For loans under the tranche D term loan that were substantially different than loans under the then existing term loans, Simmons Bedding recorded the exchange of debt instruments as a debt extinguishment, expensed deferred financing fees associated with the extinguished debt, expensed fees paid to lenders, and capitalized third-party costs associated with the New Senior Credit Facility. For loans under the tranche D term loan that were not substantially different, Simmons Bedding recorded the exchange of debt instruments as a modification of the existing term loans, expensed third-party costs associated with the New Senior Credit Facility, and capitalized fees paid to lenders as deferred financing fees. As a result of the Refinancing, Simmons Bedding expensed \$5.0 million of deferred financing fees and \$1.0 million of Refinancing Costs as a component of interest expense, net in the consolidated statements of operations and capitalized \$0.9 million of deferred financing fees as a component of other assets on the consolidated balance sheets.

The revolving loan under the New Senior Credit Facility will expire on the earlier of (a) December 19, 2009 or (b) as revolving credit commitments under the facility terminate. Simmons Bedding incurs a commitment fee of 0.5% per annum on the unused portion of its revolving credit facility. As of July 1, 2006, Simmons Bedding had availability to borrow \$65.1 million under the revolving loan after giving effect to \$9.9 million that was reserved for Simmons Bedding's reimbursement obligations with respect to outstanding letters of credit. The remaining availability under the revolving loan may be utilized to meet current working capital requirements, including issuance of stand-by and trade letters of credit. Simmons Bedding also may utilize the remaining availability under the revolving loan to fund distributions, acquisitions and capital expenditures.

Subsequent to the Refinancing, Simmons Bedding voluntarily prepaid \$12.0 million of the tranche D term loan resulting in the next required principal payment of \$0.3 million being scheduled for September 2008. The tranche D term loans have mandatory quarterly principal payments of \$1.2 million from December 31, 2008 through December 31, 2010 and mandatory quarterly principal payments of \$117.2 million from March 31, 2011 through maturity on December 19, 2011. Depending on Simmons Bedding's leverage ratio, it may be required to prepay a portion of the tranche D term loan with up to 50% of its excess cash flows (as defined in the New Senior Credit Facility) from each fiscal year.

The New Senior Credit Facility bears interest at Simmons Bedding's choice of the Eurodollar Rate or Base Rate (both as defined), plus the applicable interest rate margins as follows:

	<u>Eurodollar Rate</u>	<u>Base Rate</u>
Revolving loan	2.50%	1.50%
Tranche D term loan	2.25%	1.00%

The revolving loan applicable interest margins for both Eurodollar Rate loans and Base Rate loans are reduced based upon Simmons Bedding's leverage ratio. The weighted average interest rate per annum in effect as of July 1, 2006 for the tranche D term loan was 7.36%.

Simmons Bedding has developed and implemented a policy to utilize extended Eurodollar contracts to minimize the impact of near term Eurodollar rate increases. For \$258.0 million of the tranche D term loan, Simmons Bedding has set the interest rate utilizing twelve month Eurodollar rate loans which fixed the Eurodollar Rate at 4.875% through January 26, 2007. The execution of the extended Eurodollar contracts resulted in the Company fixing the interest rate on approximately 53% of its floating rate debt as of July 1, 2006.

The New Senior Credit Facility requires Simmons Bedding to maintain certain financial ratios, including cash interest coverage and total leverage ratios. The New Senior Credit Facility also contains other covenants, which among other things, limit capital expenditures, the incurrence of additional indebtedness, investments, dividends, transactions with affiliates, asset sales, mergers and consolidations, prepayment of other indebtedness, liens and encumbrances and other matters customarily restricted in such agreements.

Simmons Company's senior discount notes ("Discount Notes") with an aggregate principal amount at maturity of \$269.0 million bear interest at the rate of 10.0% per annum, which will be payable semi-annually in cash in arrears on June 15 and December 15 of each year commencing on June 15, 2010. Prior to December 15, 2009, interest will accrue on the Discount Notes in the form of an increase in the accreted value of the Discount Notes. The Company's ability to make payments on the Discount Notes is dependent on the earnings and distribution of funds from Simmons Bedding.

Simmons Bedding's 7.875% senior subordinated notes due 2014 are fully and unconditionally guaranteed, on a joint and several basis, and on an unsecured, senior subordinated basis by Simmons Company and THL-SC Bedding (the "Parent Guarantors") and all of the Company's active domestic subsidiaries (the "Subsidiary Guarantors"). All the Subsidiary Guarantors are 100% owned by Simmons Bedding. The following Supplemental Consolidating Condensed Financial Statements provide additional guarantor/non-guarantor information.

**Supplemental Consolidating Condensed Statements of Operations**  
**For the Quarter Ended July 1, 2006**  
(In thousands)

	Issuer and Guarantors						Eliminations	Consolidated
	Parent	Simmons		Non-Guarantor				
	Guarantors	Bedding Company	Guarantor Subsidiaries	Subsidiaries				
Net sales	\$ -	\$ (22,488)	\$ 261,469	\$ 2,220	\$ -	\$ -	\$ 241,202	
Cost of products sold	-	862	129,484	1,705	-	-	132,051	
Gross profit	-	(23,350)	131,985	515	-	-	109,151	
Operating expenses:								
Selling, general and administrative expenses	44	50,580	30,623	386	-	-	81,633	
Amortization of intangibles	-	807	610	-	-	-	1,417	
Intercompany fees	-	(77,558)	77,331	227	-	-	-	
Licensing revenues	-	(279)	(1,557)	(176)	-	-	(2,012)	
	44	(26,450)	107,007	437	-	-	81,038	
Operating income (loss)	(44)	3,100	24,978	78	-	-	28,113	
Interest expense, net	4,567	19,870	218	61	-	-	24,715	
Income from subsidiaries	5,823	21,447	-	-	(27,270)	-	-	
Income before income taxes	1,212	4,677	24,760	17	(27,270)	-	3,398	
Income tax expense (benefit)	(849)	(1,145)	3,327	3	-	-	1,337	
Net income	\$ 2,061	\$ 5,822	\$ 21,433	\$ 14	\$ (27,270)	\$ -	\$ 2,061	

**Supplemental Consolidating Condensed Statements of Operations**  
**For the Quarter Ended June 25, 2005**  
(In thousands)

	Issuer and Guarantors						Eliminations	Consolidated
	Parent	Simmons		Guarantor	Non-Guarantor			
		Guarantors	Bedding Company					
Net sales	\$ -	\$ (17,784)	\$ 222,739	\$ 3,087	\$ -	\$ -	\$ 208,042	
Cost of products sold	-	305	114,771	2,180	-	-	117,256	
Gross profit	-	(18,089)	107,968	907	-	-	90,786	
Operating expenses:								
Selling, general and administrative expenses	69	49,040	23,591	642	-	-	73,342	
Amortization of intangibles	-	807	610	-	-	-	1,417	
Intercompany fees	-	(71,072)	70,817	255	-	-	-	
Licensing revenues	-	(265)	(2,402)	(148)	-	-	(2,815)	
	69	(21,490)	92,616	749	-	-	71,944	
Operating income (loss)	(69)	3,401	15,352	158	-	-	18,842	
Interest expense, net	4,156	12,974	200	29	-	-	17,359	
Income from subsidiaries	3,679	14,173	4,162	-	(22,014)	-	-	
Income before income taxes	(546)	4,600	19,314	129	(22,014)	-	1,483	
Income tax expense (benefit)	(1,605)	920	1,266	(157)	-	-	424	
Net income	\$ 1,059	\$ 3,680	\$ 18,048	\$ 286	\$ (22,014)	\$ -	\$ 1,059	

**Supplemental Consolidating Condensed Statements of Operations**  
**For the Six Months Ended July 1, 2006**  
(In thousands)

	Issuer and Guarantors						Eliminations	Consolidated
	Parent Guarantors	Simmons		Guarantor Subsidiaries	Non-Guarantor Subsidiaries			
		Bedding Company						
Net sales	\$ -	\$ (51,740)	\$ 524,764	\$ 4,045	\$ -	\$ -	\$ 477,069	
Cost of products sold	-	1,677	263,781	3,032	-	-	268,490	
Gross profit	-	(53,417)	260,983	1,013	-	-	208,579	
Operating expenses:								
Selling, general and administrative expenses	67	93,204	58,468	800	-	-	152,539	
Amortization of intangibles	-	1,614	1,220	-	-	-	2,834	
Intercompany fees	-	(155,734)	155,346	388	-	-	-	
Licensing revenues	-	(556)	(3,391)	(353)	-	-	(4,300)	
Operating income (loss)	(67)	8,055	49,340	178	-	-	57,506	
Interest expense, net	9,225	34,148	430	88	-	-	43,891	
Income from subsidiaries	15,195	37,252	-	-	(52,447)	-	-	
Income before income taxes	5,903	11,159	48,910	90	(52,447)	-	13,615	
Income tax expense (benefit)	(2,591)	(4,035)	11,695	52	-	-	5,121	
Net income	\$ 8,494	\$ 15,194	\$ 37,215	\$ 38	\$ (52,447)	\$ -	\$ 8,494	

**Supplemental Consolidating Condensed Statements of Operations**  
**For the Six Months Ended June 25, 2005**  
(In thousands)

	Issuer and Guarantors					Eliminations	Consolidated
	Parent Guarantors	Simmons Bedding Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries			
Net sales	\$ -	\$ (33,817)	\$ 442,133	\$ 5,308	\$ -	\$ -	\$ 413,624
Cost of products sold	-	593	226,917	3,912	-	-	231,422
Gross profit	-	(34,410)	215,216	1,396	-	-	182,202
Operating expenses:							
Selling, general and administrative expenses	160	100,520	50,696	1,127	-	-	152,503
Amortization of intangibles	-	1,615	1,243	-	-	-	2,858
Intercompany fees	-	(142,807)	142,348	459	-	-	-
Licensing revenues	-	(529)	(4,009)	(328)	-	-	(4,866)
	160	(41,201)	190,278	1,258	-	-	150,495
Operating income (loss)	(160)	6,791	24,938	138	-	-	31,707
Interest expense, net	8,381	24,940	400	52	-	-	33,773
Income from subsidiaries	4,162	23,711	4,162	-	(32,035)	-	-
Income (loss) before income taxes	(4,379)	5,562	28,700	86	(32,035)	-	(2,066)
Income tax expense (benefit)	(3,246)	1,400	1,039	(126)	-	-	(933)
Net income (loss)	\$ (1,133)	\$ 4,162	\$ 27,661	\$ 212	\$ (32,035)	\$ -	\$ (1,133)

**Supplemental Consolidating Condensed Balance Sheets**  
**As of July 1, 2006**  
(In thousands)

	Issuer and Guarantors					Eliminations	Consolidated
	Parent Guarantors	Simmons Bedding Company	Subsidiary Guarantors	Non-Guarantor Subsidiaries			
<b>ASSETS</b>							
Current assets:							
Cash and cash equivalents	\$ -	\$ 18,519	\$ 7,343	\$ 3,020	\$ -	\$ -	\$ 28,882
Accounts receivable	-	-	87,365	1,129	-	-	88,494
Inventories	-	-	28,216	626	-	-	28,842
Other	-	7,077	11,127	494	-	-	18,698
<b>Total current assets</b>	<b>-</b>	<b>25,596</b>	<b>134,051</b>	<b>5,269</b>	<b>-</b>	<b>-</b>	<b>164,916</b>
Property, plant and equipment, net	-	10,741	43,395	4,939	-	-	59,075
Goodwill and other intangibles, net	-	66,090	956,486	65	-	-	1,022,641
Other assets	3,343	30,000	1,855	394	-	-	35,592
Net investment in and advances to (from) affiliates	286,765	890,031	191,799	(2,008)	(1,366,587)	-	-
	<u>\$ 290,108</u>	<u>\$ 1,022,458</u>	<u>\$ 1,327,586</u>	<u>\$ 8,659</u>	<u>\$ (1,366,587)</u>	<u>\$ -</u>	<u>\$ 1,282,224</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>							
Current liabilities:							
Current maturities of long-term debt	\$ -	\$ -	\$ 200	\$ 213	\$ -	\$ -	\$ 413
Accounts payable and accrued liabilities	145	45,037	72,658	880	-	-	118,720
<b>Total current liabilities</b>	<b>145</b>	<b>45,037</b>	<b>72,858</b>	<b>1,093</b>	<b>-</b>	<b>-</b>	<b>119,133</b>
Long-term debt	191,975	680,000	13,100	1,369	-	-	886,444
Deferred income taxes	(15,157)	(10,709)	174,548	179	-	-	148,861
Other non-current liabilities	-	9,304	5,129	208	-	-	14,641
<b>Total liabilities</b>	<b>176,963</b>	<b>723,632</b>	<b>265,635</b>	<b>2,849</b>	<b>-</b>	<b>-</b>	<b>1,169,079</b>
Stockholders' equity	113,145	298,826	1,061,951	5,810	(1,366,587)	-	113,145
	<u>\$ 290,108</u>	<u>\$ 1,022,458</u>	<u>\$ 1,327,586</u>	<u>\$ 8,659</u>	<u>\$ (1,366,587)</u>	<u>\$ -</u>	<u>\$ 1,282,224</u>

**Supplemental Consolidating Condensed Statements of Cash Flows**  
**For the Six Months Ended July 1, 2006**  
(In thousands)

	Issuer and Guarantors					Eliminations	Consolidated
	Parent Guarantors	Simmons Bedding Company	Subsidiary Guarantors	Non-Guarantor Subsidiaries			
Net cash provided by (used in) operating activities	\$ 267	\$ (15,778)	\$ 56,456	\$ 299	-	-	\$ 41,244
Cash flows from investing activities:							
Purchase of property, plant and equipment, net	-	(2,446)	(3,330)	-	-	-	(5,776)
Net cash used in investing activities	-	(2,446)	(3,330)	-	-	-	(5,776)
Cash flows from financing activities:							
Borrowings under New Senior Credit Facility, net	-	480,000	-	-	-	-	480,000
Payments of senior credit facility, net	-	(369,933)	-	-	-	-	(369,933)
Repayment of senior unsecured term loan	-	(140,000)	-	-	-	-	(140,000)
Payment of other long-term obligations	-	-	-	(106)	-	-	(106)
Purchase of treasury stock	(311)	-	-	-	-	-	(311)
Payment of financing fees	(41)	(932)	-	-	-	-	(973)
Receipt from (distribution to) affiliates	85	47,785	(47,212)	(658)	-	-	-
Net cash provided by (used in) financing activities	(267)	16,920	(47,212)	(764)	-	-	(31,323)
Net effect of exchange rate changes	-	-	-	115	-	-	115
Change in cash and cash equivalents	-	(1,304)	5,914	(350)	-	-	4,260
Cash and cash equivalents:							
Beginning of period	-	19,823	1,429	3,370	-	-	24,622
End of period	\$ -	\$ 18,519	\$ 7,343	\$ 3,020	\$ -	\$ -	\$ 28,882

**Supplemental Consolidating Condensed Statements of Cash Flows**  
**For the Six Months Ended June 25, 2005**  
(In thousands)

	Issuer and Guarantors					Eliminations	Consolidated
	Parent Guarantors	Simmons Bedding Company	Subsidiary Guarantors	Non-Guarantor Subsidiaries			
Net cash provided by (used in) operating activities	\$ (202)	\$ 4,901	\$ 14,517	\$ (870)	\$ -	\$ 18,346	
Cash flows from investing activities:							
Purchase of property, plant and equipment, net	-	(1,364)	(1,201)	(21)	-	(2,586)	
Purchase of Simmons Juvenile Products	-	-	(3,337)	-	-	(3,337)	
Net cash used in investing activities	-	(1,364)	(4,538)	(21)	-	(5,923)	
Cash flows from financing activities:							
Payments of deferred financing fees	(125)	-	-	-	-	(125)	
Repayment of long-term obligations	-	(4,667)	(41)	(118)	-	(4,826)	
Purchase of treasury stock	(304)	-	-	-	-	(304)	
Receipt from (distribution to) affiliates	279	-	(2,069)	1,790	-	-	
Net cash used in financing activities	(150)	(4,667)	(2,110)	1,672	-	(5,255)	
Net effect of exchange rate changes	-	-	-	(6)	-	(6)	
Change in cash and cash equivalents	(352)	(1,130)	7,869	775	-	7,162	
Cash and cash equivalents:							
Beginning of period	352	15,923	7,333	598	-	24,206	
End of period	\$ -	\$ 14,793	\$ 15,202	\$ 1,373	\$ -	\$ 31,368	

## F. Share-Based Compensation

Under the Simmons Company Equity Incentive Plan (“Incentive Plan”), the Company is authorized to issue 688,235 shares of Class B common stock as restricted stock awards to the management and independent directors of the Company. The restricted stock awards are performance based awards, where the restrictions lapse based upon the achievement of specific measurable performance criteria. As of January 1, 2006, most of the awards vested ratably over a four year period based upon the Company meeting certain annual Adjusted EBITDA targets or on the eighth anniversary after issuance. Future vesting was subject to the holders continued full-time employment with the Company or continuance as a director of the Company. Unvested shares accelerated upon a change of control of the Company if the Company had met certain performance criteria. Holders of the restricted stock had the right to receive dividends and vote shares, but could not sell, assign, transfer or pledge or otherwise encumber the stock.

The Company adopted the provisions of Statement of Financial Accounting Standard (“SFAS”) No. 123 (Revised 2004), *Share-Based Payment* (“SFAS 123R”) on January 1, 2006 (the first day of the 2006 first quarter). Prior to the adoption of SFAS 123R, the Company accounted for its awards of restricted stock made to its employees, directors and consultants pursuant to the Incentive Plan in accordance with the Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (“APB 25”), as permitted by SFAS No. 123, *Accounting for Stock-Based Compensation* (“SFAS 123”). Under APB 25, compensation cost was measured upon issuance of the restricted stock award as the excess of the fair value of the award over the purchase price. Fair value was determined by the Company’s board of directors based upon a quarterly valuation of the Company’s enterprise value as measured by a third party valuation specialist. The Company’s enterprise value fluctuates based upon its operating performance, changes in market multiples for comparable publicly traded companies, and changes in multiples paid for companies with similar operations as the Company. The entire amount of the compensation cost was recorded as deferred compensation and amortized as a charge to selling, general and administrative expense over the period that the restrictions were expected to lapse.

The Company used the modified prospective application method of transition under SFAS 123R. Under the modified prospective application method, the Company will apply SFAS 123R for new awards granted after January 1, 2006 and for unvested awards as of January 1, 2006. Upon adoption of SFAS 123R, the Company made a one-time cumulative adjustment to record an estimate of the future forfeitures on all outstanding restricted stock awards. Additionally, the Company netted its deferred compensation related to awards issued prior to the adoption of SFAS 123R against additional paid in capital. Under SFAS 123R, compensation cost is measured at the grant date as the excess of the fair value of the award over the purchase price. Fair value is determined by the Company’s board of directors based upon a quarterly valuation of the Company’s enterprise value as measured by a third party valuation specialist.

Since vesting of certain restricted stock awards granted under the Incentive Plan was unlikely, 569,136 shares of restricted stock awards were modified by the Company on April 17, 2006. Among other things, the modification resulted in the vesting of 18.75% of restricted stock awards for certain individuals not previously vested; revising of the vesting schedule through 2008; lowering of the Adjusted EBITDA performance targets for 2006 and 2007; and the elimination of cliff vesting. The fair value of the restricted stock awards post-modification was greater than the fair value of the awards prior to modification. As a result, the Company recorded an additional \$1.0 million of deferred compensation, which will be recognized as an expense over the modified three year graded vesting schedule.

The following table presents a rollforward of the number of nonvested shares for the six months ended July 1, 2006 and the weighted-average grant-date fair value of the restricted stock awards:

	<b>Number of Shares</b>	<b>Weighted Average Fair Value at Grant Date</b>
Nonvested shares as of December 31, 2005	536,652	\$ 0.84
Granted	84,850	\$ 2.43
Vested	(26,287)	\$ 3.19
Forfeited	(95,561)	\$ 0.67
Nonvested shares as of July 1, 2006	<u>499,654</u>	<u>\$ 1.01</u>

Non-cash stock compensation expense was \$0.5 million for the quarter and six months ended July 1, 2006 and zero for the quarter and six months ended June 25, 2005. As of July 1, 2006, there was \$1.0 million of total unrecognized compensation cost related to nonvested restricted stock awards granted under the Incentive Plan which is expected to be recognized as an expense over a weighted average period of 2.6 years.

#### **G. Segment Information**

Operating segments are generally organized internally by whether the products are sold to a reseller or to an end consumer. The Company has aggregated similar operating segments into two reportable segments: (1) wholesale bedding and (2) retail bedding.

The wholesale bedding segment consists of (i) the manufacture, sale and distribution of premium branded bedding products to retail customers and institutional users of bedding products, such as the hospitality industry; (ii) the manufacture, sale and distribution of juvenile bedding and related soft good products; (iii) the licensing of intellectual property to domestic and international companies that manufacture and sell the Company's premium branded bedding products or products which complement the bedding products manufactured by the Company and its licensees; (iv) the sale of product returns, off-quality product and excess inventory to "as-is" dealers and to consumers through the Company's owned retail outlet stores; and (v) corporate costs related to the Company.

The retail bedding segment currently operates specialty sleep stores under the Sleep Country USA name in Oregon and Washington that principally sell premium branded bedding products to consumers. On July 24, 2006, the Company entered into a definitive purchase agreement with an affiliate of Sleep Train, Inc. to sell Sleep Country USA, Inc. (see note I - Subsequent Event). The transaction is expected to close in August of 2006. Subsequent to the transaction, the Company will only have one reportable segment, the wholesale bedding segment.

The Company evaluates segment performance and allocates resources based on net sales and Adjusted EBITDA. Adjusted EBITDA differs from the term "EBITDA" as it is commonly used. In addition to adjusting net income to exclude interest expense, income taxes, depreciation and amortization, Adjusted EBITDA also adjusts net income by excluding items or expenses not typically excluded in the calculation of "EBITDA" such as management fees and unusual or non-recurring items as defined by the Company's senior credit facility. Management believes the aforementioned approach is the most informative representation of how management evaluates performance. Adjusted EBITDA does not represent net income or cash flow from operations as those terms are defined by GAAP and does not necessarily indicate whether cash flows will be sufficient to fund cash needs.

The following tables summarize segment information:

**Quarter Ended July 1, 2006**  
(In thousands)

	Wholesale Bedding	Retail	Eliminations	Totals
Net sales to external customers	\$ 218,260	\$ 22,942	\$ -	\$ 241,202
Intersegment net sales	4,409	-	(4,409)	-
Adjusted EBITDA	35,438	1,843	43	37,324
Depreciation and amortization expense	6,446	331	-	6,777
Expenditures for long-lived assets	1,786	682	-	2,468
Segment assets	1,258,499	25,217	(1,492)	1,282,224

Reconciliation of EBITDA and Adjusted EBITDA to net income:

Net income	\$ 1,034	\$ 984	\$ 43	\$ 2,061
Depreciation and amortization	6,446	331	-	6,777
Income taxes	1,012	325	-	1,337
Interest expense, net	24,715	-	-	24,715
Interest income	151	-	-	151
EBITDA	33,358	1,640	43	35,041
Reorganization costs	728	-	-	728
Non-cash stock compensation	515	-	-	515
Management fees	326	115	-	441
State taxes in lieu of income taxes	153	88	-	241
Transaction expenses	133	-	-	133
Management severance	101	-	-	101
Other	124	-	-	124
Adjusted EBITDA	<u>\$ 35,438</u>	<u>\$ 1,843</u>	<u>\$ 43</u>	<u>\$ 37,324</u>

**Quarter Ended June 25, 2005**

(In thousands)

	Wholesale			Totals
	Bedding	Retail	Eliminations	
Net sales to external customers	\$ 189,283	\$ 18,759	\$ -	\$ 208,042
Intersegment net sales	3,414	-	(3,414)	-
Adjusted EBITDA	25,890	1,606	95	27,591
Depreciation and amortization expense	6,234	427	-	6,661
Expenditures for long-lived assets	1,032	176	-	1,208
Segment assets	1,263,943	27,406	(1,505)	1,289,844
Reconciliation of EBITDA and Adjusted EBITDA to net income:				
Net income	\$ 320	\$ 644	\$ 95	\$ 1,059
Depreciation and amortization	6,234	427	-	6,661
Income taxes	57	367	-	424
Interest expense, net	17,356	3	-	17,359
Interest income	20	1	-	21
EBITDA	23,987	1,442	95	25,524
Reorganization costs	1,345	-	-	1,345
Management fees	238	94	-	332
Transaction expenses	177	-	-	177
State taxes in lieu of income taxes	103	70	-	173
Other	40	-	-	40
Adjusted EBITDA	<u>\$ 25,890</u>	<u>\$ 1,606</u>	<u>\$ 95</u>	<u>\$ 27,591</u>

**Six Months Ended July 1, 2006**  
(In thousands)

	Wholesale			Totals
	Bedding	Retail	Eliminations	
Net sales to external customers	\$ 430,492	\$ 46,577	\$ -	\$ 477,069
Intersegment net sales	9,124	-	(9,124)	-
Adjusted EBITDA	71,703	4,547	22	76,272
Depreciation and amortization expense	13,408	649	-	14,057
Expenditures for long-lived assets	4,400	1,376	-	5,776
Segment assets	1,258,499	25,217	(1,492)	1,282,224
Reconciliation of EBITDA and Adjusted EBITDA to net income:				
Net income	\$ 6,114	\$ 2,358	\$ 22	\$ 8,494
Depreciation and amortization	13,408	649	-	14,057
Income taxes	3,995	1,126	-	5,121
Interest expense, net	43,887	4	-	43,891
Interest income	235	-	-	235
EBITDA	67,639	4,137	22	71,798
Reorganization costs	1,454	-	-	1,454
Management severance	927	-	-	927
Management fees	613	233	-	846
Non-cash stock compensation	517	-	-	517
State taxes in lieu of income taxes	311	177	-	488
Transaction expenses	133	-	-	133
Other	109	-	-	109
Adjusted EBITDA	\$ 71,703	\$ 4,547	\$ 22	\$ 76,272

**Six Months Ended June 25, 2005**

(In thousands)

	Wholesale			
	Bedding	Retail	Eliminations	Totals
Net sales to external customers	\$ 375,734	\$ 37,890	\$ -	\$ 413,624
Intersegment net sales	6,563	-	(6,563)	-
Adjusted EBITDA	43,609	3,790	242	47,641
Depreciation and amortization expense	12,369	752	-	13,121
Expenditures for long-lived assets	2,156	430	-	2,586
Segment assets	1,263,943	27,406	(1,505)	1,289,844
Reconciliation of EBITDA and Adjusted EBITDA to net income (loss):				
Net income (loss)	\$ (3,114)	\$ 1,739	\$ 242	\$ (1,133)
Depreciation and amortization	12,369	752	-	13,121
Income taxes	(1,898)	965	-	(933)
Interest expense, net	33,769	4	-	33,773
Interest income	58	1	-	59
EBITDA	41,184	3,461	242	44,887
Reorganization costs	1,345	-	-	1,345
Management fees	562	190	-	752
State taxes in lieu of income taxes	196	139	-	335
Transaction expenses	177	-	-	177
Management severance	105	-	-	105
Other	40	-	-	40
Adjusted EBITDA	\$ 43,609	\$ 3,790	\$ 242	\$ 47,641

**H. Contingencies**

From time to time, the Company has been involved in various legal proceedings. The Company believes that all current litigation is routine in nature and incidental to the conduct of the Company's business, and that none of this litigation, if determined adversely to the Company, would have a material adverse effect on the Company's financial condition or results of its operations.

**I. Subsequent Event**

On July 24, 2006, the Company entered into a definitive purchase agreement to sell Sleep Country USA, Inc. ("Sleep Country"), its retail bedding segment, to an affiliate of Sleep Train, Inc. ("Sleep Train") for cash proceeds of approximately \$55 million. The transaction is anticipated to close in August of 2006. Separately, the Company agreed to enter into a multi-year supply agreement with the combined Sleep Country and Sleep Train entities.

## J. Accounting Pronouncements

In February 2006, the Financial Accounting Standards Board (“FASB”) issued SFAS No. 155, *Accounting for Certain Hybrid Instruments* (“SFAS 155”). SFAS 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. SFAS 155 will be effective for all financial instruments acquired or issued by the Company beginning in fiscal year 2007. The Company does not have any financial instruments with embedded derivatives and does not expect this statement to have a significant impact on its consolidated financial statements or results of operations.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets - An Amendment of FASB Statement No. 140* (“SFAS 156”). Among other requirements, SFAS 156 provides guidance on the accounting for servicing assets or liabilities when an entity undertakes an obligation to service a financial asset by entering into a service contract. SFAS 156 will be effective for the Company at the beginning of fiscal year 2007. The Company does not expect this statement to have a significant impact on its consolidated financial statements or results of operations.

In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109* (“FIN 48”). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 will be effective for the Company at the beginning of fiscal year 2007. The Company is in the process of evaluating the impact of this guidance on its consolidated financial statements and results of operations.

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

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our audited consolidated financial statements as of December 31, 2005, including related notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our 2005 Annual Report on Form 10-K, and the unaudited interim financial statements included elsewhere in this report.

### **Recent Events**

#### *Sale of Retail Segment*

On July 24, 2006, we entered into a definitive purchase agreement to sell Sleep Country USA, Inc. ("Sleep Country"), our retail bedding segment, to an affiliate of Sleep Train, Inc. ("Sleep Train") for cash proceeds of approximately \$55 million. The transaction is anticipated to close in August of 2006. Separately, we agreed to enter into a multi-year supply agreement with the combined Sleep Country and Sleep Train entities.

## Results of Operations

The following table sets forth historical consolidated financial information as a percent of net sales:

	Quarters Ended		Six Months Ended	
	July 1, 2006	June 25, 2005	July 1, 2006	June 25, 2005
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of products sold	54.7%	56.4%	56.3%	55.9%
Gross margin	45.3%	43.6%	43.7%	44.1%
Operating expenses:				
Selling, general and administrative expenses	33.8%	35.3%	32.0%	36.9%
Amortization of intangibles	0.6%	0.7%	0.6%	0.7%
Licensing revenues	(0.8%)	(1.4%)	(0.9%)	(1.2%)
	33.7%	34.5%	31.6%	36.3%
Operating income	11.6%	9.1%	12.1%	7.8%
Interest expense, net	10.2%	8.3%	9.2%	8.2%
Income (loss) before income taxes	1.4%	0.8%	2.9%	(0.4%)
Income tax expense (benefit)	0.6%	0.2%	1.1%	(0.2%)
Net income (loss)	0.8%	0.6%	1.8%	(0.2%)

### Quarter Ended July 1, 2006 as Compared to the Quarter Ended June 25, 2005

*Net Sales.* The following table presents our net sales and the dollar amount and percentage change by segment for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005.

	2006	2005	\$ increase (decrease)	% increase (decrease)
			(in millions)	
Wholesale bedding segment	\$ 222.7	\$ 192.7	\$ 30.0	15.6%
Retail bedding segment	22.9	18.7	4.2	22.3%
Eliminations	(4.4)	(3.4)	(1.0)	29.1%
Consolidated net sales	\$ 241.2	\$ 208.0	\$ 33.2	15.9%

For the quarter ended July 1, 2006, wholesale bedding segment net sales increased 15.6% compared to the same period a year ago primarily as a result of (i) a 13.8% increase in our conventional bedding unit volume resulting in an estimated increase in wholesale bedding net sales of \$28.0 million and (ii) a 2.4% increase in our conventional bedding average unit selling price ("AUSP") resulting in an estimated increase of wholesale bedding net sales of \$5.6 million. Our conventional bedding unit volume increase resulted principally from the remerchandising of our product lines with our dealers primarily in the second and third quarters of 2005 to include better product offerings at key retail price points. Our improvement in AUSP in the second quarter was primarily attributable to the price increase implemented during the fourth quarter of 2005 to help minimize the impact of rising raw material costs, partially offset by a change in our sales mix.

For the quarters ended July 1, 2006 and June 25, 2005, our wholesale bedding segment net sales reflect a reduction of \$20.2 million and \$17.7 million, respectively, for cash consideration paid to our customers for certain promotional programs, allowances and volume rebates. Our sales reductions increased for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005 principally due to (i) an increase in special promotional allowances of \$1.5 million related to second quarter 2006 sales events at certain of our dealers and (ii) a \$1.1 million increase of co-op advertising expenditures, recorded as a sales reduction, due to our increase in sales. As a percentage of our sales, our overall co-op advertising expenditures, regardless of whether reported as selling expense or a sales reduction, for the quarter ended July 1, 2006, were 0.1 percentage points higher than the overall co-op advertising expenditures for the quarter ended June 25, 2005.

Retail bedding segment net sales increased \$4.2 million, or 22.3%, for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005 as a result of the net addition of nine new retail stores and increased same store sales. On a comparable store basis, sales for our retail stores increased 3.4% for the quarter ended July 1, 2006 versus the quarter ended June 25, 2005. Retail segment same store sales benefited from a rise in the average retail sales transaction due to an increase in retail prices and a shift in sales mix.

*Gross Margin.* The following table presents our gross profit, gross margin, and the gross margin percentage point change by segment for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005.

	Gross Profit		Gross Margin		Margin %
	2006	2005	2006	2005	Point Change
	(in millions)				
Wholesale bedding segment	\$ 96.6	\$ 80.7	43.4%	41.9%	1.5%
Retail bedding segment	12.5	10.0	54.3%	53.1%	1.2%
Eliminations	0.0	0.1	(1.0%)	(2.8%)	1.8%
Consolidated	<u>\$ 109.1</u>	<u>\$ 90.8</u>	45.3%	43.6%	1.7%

Our wholesale bedding segment gross margin for the quarter ended July 1, 2006, increased by 1.5 percentage points compared to the quarter ended June 25, 2005, primarily due to an 8.1% decrease in our conventional bedding labor and overhead cost per unit resulting from favorable efficiencies driven by our increased unit volume. Partially offsetting the improvement in labor and overhead cost per unit, our conventional bedding material cost per unit increased 3.3% for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005 due to inflation in raw material costs.

Our retail bedding segment gross margin increased 1.2 percentage points principally due to a shift in sales mix to higher margin products during the second quarter of 2006 compared to the second quarter of 2005.

*Selling, general and administrative expenses ("SG&A").* The following table presents our SG&A by dollar amount, as a percentage of net sales and the percentage point change by segment for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005.

	SG&A		As a % of Segment Net Sales		Margin %
	2006	2005	2006	2005	Point Change
	(in millions)				
Wholesale bedding segment	\$ 70.6	\$ 64.5	31.7%	33.5%	(1.8%)
Retail bedding segment	11.1	8.9	48.3%	47.2%	1.1%
Consolidated	\$ 81.6	\$ 73.3	33.8%	35.3%	(1.5%)

As a percentage of wholesale bedding segment net sales, our wholesale bedding segment SG&A for the quarter ended July 1, 2006 declined 1.8 percentage points compared to the quarter ended June 25, 2005. SG&A decreased principally due to lower selling expenses, which decreased \$3.6 million, or 3.0 percentage points, primarily as a result of our sales force reorganization in December 2005 and the timing of new product introductions. Partially offsetting our lower selling expenses, our general and administrative expenses increased \$3.8 million, or 0.7 percentage points, principally due to higher bonus and non-cash stock compensation expense as a result of our improved operating performance, and our national advertising expenses increased \$2.2 million, or 0.7 percentage points, due to the timing of our 2006 national advertising campaign in comparison to the same period last year.

Our retail segment SG&A increased 1.1 percentage points for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005 primarily due to the addition of the nine new stores, higher bonus expense, and a company training event.

*Amortization of Intangibles.* For each of the quarters ended July 1, 2006 and June 25, 2005, amortization of intangibles was \$1.4 million.

*Licensing Revenues.* For the quarter ended July 1, 2006, licensing fees decreased \$0.8 million to \$2.0 million from \$2.8 million for the quarter ended June 25, 2005. Licensing fees for the quarter ended June 25, 2005 included additional royalties of \$0.6 million resulting from an audit of a licensee.

*Interest Expense, Net.* For the quarter ended July 1, 2006, interest expense increased \$7.4 million to \$24.7 million from \$17.4 million for the quarter ended June 25, 2005. Interest expense increased principally due to the expensing of \$5.0 million of deferred financing fees associated with the tranche C and senior secured term loans that were extinguished in connection with Simmons Bedding's borrowing of \$492 million in May 2006 under a tranche D term loan (the "Refinancing"). Additionally, in connection with the Refinancing, Simmons Bedding incurred \$1.0 million of refinancing costs that were recorded as interest expense. Excluding the expenses associated with the Refinancing, interest expense for the quarter ended July 1, 2006 compared to the quarter ended June 25, 2005 increased \$1.4 million due primarily to higher LIBOR base rates on our senior credit facility, partially offset by lower average outstanding borrowings and reduced interest rate margins for our senior credit facility as a result of the Refinancing. Our non-cash interest expense for the quarter ended July 1, 2006 was \$10.1 million, which included \$5.0 million of deferred financing fees expensed as a result of the Refinancing and \$4.5 million related to the amortization of the original issuance discount on our 10% senior discount notes.

*Income Taxes.* The combined federal, state and foreign effective income tax rate for the quarter ended July 1, 2006 of 39.3% differs from the federal statutory rate of 35.0% primarily due to state income tax expense. The combined federal, state and foreign effective income tax rate for the quarter ended June 25, 2005 of 28.6% differs from the federal statutory rate of 35.0% primarily due to (i) tax benefits realized as a result of a decrease in the rate applicable to our Puerto Rico subsidiary's deferred tax assets and liabilities and (ii) state income tax expense.

#### Six Months Ended July 1, 2006 as Compared to the Six Months Ended June 25, 2005

*Net Sales.* The following table presents our net sales and the dollar amount and percentage change by segment for the six months ended July 1, 2006 compared to the six months ended June 25, 2005.

	2006	2005	\$ increase (decrease)	% increase (decrease)
	(in millions)			
Wholesale bedding segment	\$ 439.6	\$ 382.3	\$ 57.3	15.0%
Retail bedding segment	46.6	37.9	8.7	22.9%
Eliminations	(9.1)	(6.6)	(2.5)	39.4%
Consolidated net sales	\$ 477.1	\$ 413.6	\$ 63.5	15.3%

For the six months ended July 1, 2006, wholesale bedding segment net sales increased 15.0% compared to the same period a year ago primarily as a result of (i) a 14.2% increase in our conventional bedding unit volume resulting in an estimated increase in wholesale bedding net sales of \$57.1 million and (ii) a 2.8% increase in our conventional bedding AUSP resulting in an estimated increase of wholesale bedding net sales of \$12.7 million. Our conventional bedding unit volume increase resulted principally from the remerchandising of our product lines with our dealers primarily in the second and third quarters of 2005 to include better product offerings at key retail price points. Our improvement in AUSP was primarily attributable to the price increase implemented during the fourth quarter of 2005 to help minimize the impact of rising raw material costs, partially offset by a change in our sales mix.

Partially offsetting the six months wholesale bedding segment net sales increase, our sales reductions for cash consideration paid to our customers for certain promotional programs, allowances and volume rebates increased \$12.4 million to \$47.1 million for the six months ended July 1, 2006 compared to \$34.7 million for the six months ended June 25, 2005. Our sales reductions increased for the six months ended July 1, 2006 compared to the six months ended June 25, 2005 principally due to (i) an \$8.9 million increase resulting from our increase in sales and dealers providing less proof of advertising for the co-op subsidies they receive from us, which resulted in more co-op advertising expenditures being recorded as a sales reduction versus a selling expense and (ii) an increase in special promotional allowances of \$2.1 million related to 2006 sales events at certain of our dealers during the first six months of 2006. As a percentage of our sales, our overall co-op advertising expenditures, regardless of whether reported as selling expense or a sales reduction, for the six months ended July 1, 2006, was 0.6 percentage points higher than the overall co-op advertising expenditures for the six months ended June 25, 2005, due to a shift in product and sales mix to dealers that receive more subsidies.

Retail bedding segment net sales increased \$8.7 million, or 22.9%, for the six months ended July 1, 2006 compared to the six months ended June 25, 2005 as a result of the net addition of nine new retail stores and increased same store sales. On a comparable store basis, sales for our retail stores increased 6.5% for the six months ended July 1, 2006 versus the six months ended June 25, 2005. Retail segment same store sales benefited from a rise in the average retail sales transaction due to an increase in retail prices and a shift in sales mix.

*Gross Margin.* The following table presents our gross profit, gross margin, and the gross margin percentage point change by segment for the six months ended July 1, 2006 compared to the six months ended June 25, 2005.

	Gross Profit		Gross Margin		Margin %
	2006	2005	2006	2005	Point Change
	(in millions)				
Wholesale bedding segment	\$ 183.6	\$ 161.7	41.8%	42.3%	(0.5%)
Retail bedding segment	24.9	20.2	53.5%	53.4%	0.1%
Eliminations	0.0	0.2	(0.2%)	(3.7%)	3.5%
Consolidated	\$ 208.6	\$ 182.2	43.7%	44.1%	(0.4%)

Our wholesale bedding segment gross margin for the six months ended July 1, 2006, declined by 0.5 percentage points compared to the six months ended June 25, 2005, principally due to (i) a 6.2% increase in our conventional bedding material cost per unit resulting from inflation in raw material costs and (ii) a \$12.4 million increase in our sales reductions (see above "Net Sales" discussion). Partially offsetting these decreases, our conventional bedding labor and overhead cost per unit decreased 8.3% for the six months ended July 1, 2006 compared to the six months ended June 25, 2005 as a result of favorable efficiencies driven by our increased unit volume.

SG&A. The following table presents our SG&A by dollar amount, as a percentage of net sales and the percentage point change by segment for the six months ended July 1, 2006 compared to the six months ended June 25, 2005.

	SG&A		As a % of Segment Net Sales		Margin %
	2006	2005	2006	2005	Point Change
	(in millions)				
Wholesale bedding segment	\$ 131.3	\$ 135.1	29.9%	35.4%	(5.5%)
Retail bedding segment	21.3	17.4	45.7%	45.8%	(0.1%)
Consolidated	\$ 152.5	\$ 152.5	32.0%	36.9%	(4.9%)

As a percentage of wholesale bedding segment net sales, our wholesale bedding segment SG&A for the six months ended July 1, 2006 declined 5.5 percentage points compared to the six months ended June 25, 2005. SG&A decreased principally due to reductions (i) in our selling expenses of \$8.9 million, or 3.5 percentage points, primarily as a result of our sales force reorganization and the timing of new product introductions; (ii) our advertising expenses of 1.3 percentage points, principally due to the classification of more co-op advertising expenditures as a reduction of net sales as discussed above under "Net Sales" and less national advertising; and (iii) our corporate function expenses of \$2.2 million, or 0.6 percentage points, due to our bi-annual national leadership meeting having occurred in the first six months of 2005, whereas no such event occurred in 2006.

*Amortization of Intangibles.* For each of the six months ended July 1, 2006 and June 25, 2005, amortization of intangibles was \$2.8 million.

*Licensing Revenues.* For the six months ended July 1, 2006, licensing fees decreased \$0.6 million to \$4.3 million from \$4.9 million for the six months ended June 25, 2005. Licensing fees for the six months ended June 25, 2005 included additional royalties of \$0.6 million related to an audit of a licensee.

*Interest Expense, Net.* For the six months ended July 1, 2006, interest expense increased \$10.1 million to \$43.9 million from \$33.8 million for the six months ended June 25, 2005. Interest expense increased principally due to the expensing of \$5.0 million of deferred financing fees associated with the Refinancing. Additionally, in connection with the Refinancing, Simmons Bedding incurred \$1.0 million of refinancing costs that were recorded as interest expense. Excluding the expenses related to the Refinancing, interest expense for the six months ended July 1, 2006 compared to the six months ended June 25, 2005 increased \$4.1 million due primarily to higher LIBOR base rates on our senior credit facility, partially offset by lower average outstanding borrowings and reduced interest rate margins for our senior credit facility as a result of the Refinancing. Our non-cash interest expense for the six months ended July 1, 2006 was \$15.7 million, which included \$9.1 million related to the amortization of the original issuance discount on our 10% senior discount notes and \$5.0 million of deferred financing fees expensed as a result of the Refinancing.

*Income Taxes.* The combined federal, state, and foreign effective income tax rate for the six months ended July 1, 2006 of 37.6%, differs from the federal statutory rate of 35.0% primarily due to state income tax expense. The combined federal, state, and foreign effective income tax rate for the six months ended June 25, 2005 of 45.2% differs from the federal statutory rate of 35.0% primarily due to (i) tax benefits realized as a result of a decrease in the rate applicable to our Puerto Rico subsidiary's deferred tax assets and liabilities and (ii) state income tax expense.

## Liquidity and Capital Resources

Simmons Company is a holding company and, as a result, its primary sources of funds are cash generated from the operating activities of its indirect operating subsidiary, Simmons Bedding, and from borrowings by Simmons Bedding. Restrictive covenants in Simmons Bedding's debt agreements restrict its ability to pay cash dividends and make other distributions to Simmons Company.

Simmons Bedding's principal sources of cash to fund liquidity needs are (i) cash provided by operating activities and (ii) borrowings available under its senior credit facility. Simmons Bedding's primary uses of funds consists of payments of funding for working capital increases, principal and interest payments for Simmons Bedding's debt, capital expenditures, customer supply agreements and acquisitions. Barring any unexpected significant external or internal developments, we expect current cash balances on hand, cash provided by operating activities and borrowings available under Simmons Bedding's senior credit facility to be sufficient to meet Simmons Bedding's short-term and long-term liquidity needs.

On May 25, 2006, Simmons Bedding executed the second amended and restated senior credit and guaranty agreement ("New Senior Credit Facility") with a syndicate of lenders, which amends and restates its existing senior credit facility in its entirety. The New Senior Credit Facility provides for a \$75.0 million revolving credit facility and a \$492.0 million tranche D term loan facility. The proceeds from the New Senior Credit Facility were used to replace Simmons Bedding's \$350.0 million tranche C term loan and \$140.0 million senior unsecured term loan. This exchange of debt instruments is referred to as the "Refinancing". Among other things, the New Senior Credit Facility reduces the applicable Eurodollar and Base interest rate margins for borrowings under the term loan. Subsequent to the Refinancing, Simmons Bedding voluntarily prepaid \$12.0 million of the tranche D term loan resulting in the next required principal payment of \$0.3 million being scheduled for September 2008.

Future principal payments of our debt are expected to be paid out of cash flow from operations, borrowings available under the senior credit facility or proceeds from the sale of assets. Historically, we have paid minimal federal income taxes as a result of net operating loss carryforwards. For 2006, we had net operating loss carryforwards for federal income tax purposes of \$123.1 million and state net operating loss carryforwards of \$95.8 million. Our federal and state net operating loss carryforwards expire on various dates through 2024 and 2025, respectively. As a result of our net operating losses, we expect to pay minimal federal and state income taxes in 2006.

The following table summarizes our changes in cash (in millions):

	Six Months Ended	
	July 1, 2006	June 25, 2005
<b>Statement of Cash Flow Data:</b>		
Cash flows provided by (used in):		
Operating activities	\$ 41.2	\$ 18.3
Investing activities	(5.8)	(5.9)
Financing activities	(31.3)	(5.2)
Net effect of exchange rates	0.1	-
<b>Increase in cash and cash equivalents</b>	<b>4.2</b>	<b>7.2</b>
Cash and cash equivalents:		
Beginning of period	24.7	24.2
End of period	<u>\$ 28.9</u>	<u>\$ 31.4</u>

**Six Months Ended July 1, 2006 as Compared to Six Months Ended June 25, 2005**

*Cash flows provided by Operating Activities.* Our cash flows from operating activities increased \$22.9 million for the six months ended July 1, 2006 compared to the six months ended June 25, 2005 primarily due to increased cash flows resulting from our increase in net sales and our lower cost structure. Our working capital as a percentage of last twelve months net sales decreased to 1.8% as of July 1, 2006 compared to 1.9% as of December 31, 2005.

*Cash flows used in Investing Activities.* Our cash flows used in investing activities decreased \$0.1 million for the six months ended July 1, 2006 compared to the six months ended June 25, 2005. We paid \$3.3 million of contingent cash consideration related to the acquisition of certain assets of Simmons Juvenile Products, Inc. (“Juvenile Acquisition”) during the first six months of 2005. Exclusive of the Juvenile Acquisition, cash flows used in investing activities increased \$3.2 million principally due to the upgrade of our computer systems software.

*Cash flows used in Financing Activities.* Our cash flows used in financing activities increased \$26.1 million during the six months ended July 1, 2006 compared to the six months ended June 25, 2005 principally due to more voluntary payments on our senior credit facility. For the first six months of 2006, we have repaid \$30.0 million of debt (net of borrowings) compared to \$4.8 million for the first six months of 2005.

**Debt**

The New Senior Credit Facility provides for a \$75.0 million revolving loan and a \$492.0 million tranche D term loan facility. The revolving loan will expire on the earlier of (a) December 19, 2009 or (b) as revolving credit commitments under the facility terminate. Simmons Bedding incurs a commitment fee of 0.5% per annum on the unused portion of its revolving credit facility. As of July 1, 2006, Simmons Bedding had availability to borrow \$65.1 million under the revolving loan after giving effect to \$9.9 million that was reserved for Simmons Bedding’s reimbursement obligations with respect to outstanding letters of credit. The remaining availability under the revolving loan may be utilized to meet Simmons Bedding’s current working capital requirements, including issuance of stand-by and trade letters of credit. Simmons Bedding also may utilize the remaining availability under the revolving loan to fund distributions, acquisitions and capital expenditures.

Prior to the Refinancing, Simmons Bedding prepaid \$19.9 million of its tranche C term loan. Subsequent to the Refinancing, Simmons Bedding voluntarily prepaid \$12.0 million of the tranche D term loan resulting in the next required principal payment of \$0.3 million being scheduled for September 2008. The tranche D term loans have mandatory quarterly principal payments of \$1.2 million from December 31, 2008 through December 31, 2010 and mandatory quarterly principal payments of \$117.2 million from March 31, 2011 through maturity on December 19, 2011. Depending on Simmons Bedding's leverage ratio, Simmons Bedding may be required to prepay a portion of the tranche D term loan with up to 50% of Simmons Bedding's excess cash flows (as defined in the New Senior Credit Facility) from each fiscal year.

The New Senior Credit Facility bears interest at Simmons Bedding's choice of the Eurodollar Rate or Base Rate (both as defined), plus the applicable interest rate margins as follows:

	<u>Eurodollar Rate</u>	<u>Base Rate</u>
Revolving loan	2.50%	1.50%
Tranche D term loan	2.25%	1.00%

The revolving loan applicable interest margins for both Eurodollar Rate loans and Base Rate loans are reduced based upon Simmons Bedding's leverage ratio. The weighted average interest rate per annum in effect as of July 1, 2006 for the tranche D term loan was 7.36%.

Simmons Bedding has developed and implemented a policy to utilize extended Eurodollar contracts to minimize the impact of near term Eurodollar rate increases. For \$258.0 million of the tranche D term loan, Simmons Bedding set the interest rate utilizing twelve month Eurodollar rate loans which fixed the Eurodollar Rate at 4.875% through January 26, 2007. The execution of extended Eurodollar contracts resulted in Simmons Bedding fixing the interest rate on approximately 53% of its floating rate debt.

Simmons Company's and Simmons Bedding's long-term obligations contain various financial tests and covenants. Simmons Company and Simmons Bedding were in compliance with such covenants as of July 1, 2006. However, if Simmons Bedding's operating results fall below current expectations, Simmons Company or Simmons Bedding may not be able to meet such covenants in future periods. If Simmons Company or Simmons Bedding are not in compliance with such covenants in future periods we would be required to obtain a waiver from our lenders to avoid being in default. Simmons Bedding may not be able to obtain such a waiver on a timely basis or at all. The most restrictive covenants apply to Simmons Bedding and relate to ratios of Adjusted EBITDA to interest coverage (interest coverage ratio) and total net debt (debt less cash) to Adjusted EBITDA (leverage ratio), all as defined in Simmons Bedding's senior credit facility. The minimum cash interest coverage ratio and maximum leverage ratios are computed based on Simmons Bedding's results for the last twelve months ended, adjusted for any dispositions or acquisitions. The senior credit facility covenants also contain a maximum capital expenditure limitation of \$30.0 million per fiscal year, with the ability to roll forward to future years unused amounts from the previous fiscal year, and also subject to adjustments for certain acquisitions and dispositions. More specifically, Simmons Bedding's financial covenants related to minimum cash interest coverage ratio and maximum leverage ratios, as amended, are as follows:

- A minimum cash interest coverage ratio, with compliance levels ranging from cash interest coverage of no less than 1.85:1.00 from July 1, 2006 through December 31, 2006; 2.00:1.00 as of March 31, 2007; 2.15:1.00 from June 30, 2007 through September 30, 2007; 2.25:1.00 as of December 31, 2007; 2.75:1.00 from March 31, 2008 through December 31, 2008; and 3.00:1.00 from March 31, 2009 through each fiscal quarter thereafter.
- A maximum leverage ratio, with compliance levels ranging from total leverage of no greater than 6.25:1.00 as of July 1, 2006; 6.15:1.00 as of September 30, 2006; 5.90:1.00 as of December 31, 2006; 5.60:1.00 as of March 31, 2007; 5.25:1.00 as of June 30, 2007; 5.00:1.00 from September 30, 2007 through December 31, 2007; 4.50:1.00 from March 31, 2008 through December 31, 2008; and 4.00:1.00 from March 31, 2009 through each fiscal quarter ending thereafter.

Adjusted EBITDA (as defined in Simmons Bedding's senior credit facility) differs from the term "EBITDA" as it is commonly used. In addition to adjusting net income to exclude interest expense, income taxes, depreciation and amortization, Adjusted EBITDA also adjusts net income by excluding items or expenses not typically excluded in the calculation of "EBITDA" such as management fees; other non-cash items reducing consolidated net income (including, without limitation, non-cash purchase accounting adjustments and debt extinguishment costs); any extraordinary, unusual, or non-recurring gains or losses or charges or credits; and any reasonable expenses or charges related to any issuance of securities, investments permitted, permitted acquisitions, recapitalizations, asset sales permitted or indebtedness permitted to be incurred, less other non-cash items increasing consolidated net income, all of the foregoing as determined on a consolidated basis for Simmons Bedding in conformity with GAAP. Adjusted EBITDA is presented herein because it is a material component of the covenants contained within the aforementioned credit agreements. Non-compliance with such covenants could result in the requirement to immediately repay all amounts outstanding under such agreements, which could have a material adverse effect on our results of operations, financial position and cash flow. While the determination of "unusual and nonrecurring losses" is subject to interpretation and requires judgment, we believe the Adjusted EBITDA presented below is in accordance with the senior credit facility. Adjusted EBITDA does not represent net income or cash flow from operations as those terms are defined by GAAP and does not necessarily indicate whether cash flows will be sufficient to fund cash needs.

The following is a calculation of Simmons Bedding's minimum cash interest coverage and maximum leverage ratios under its senior credit facility as of July 1, 2006 (dollar amounts in millions, except ratios). The terms and related calculations are defined in Simmons Bedding's senior credit facility.

	<b>July 1, 2006</b>
<b>Calculation of minimum cash interest coverage ratio:</b>	
Simmons Bedding twelve months ended adjusted EBITDA(1)	\$ 143.2
Simmons Bedding consolidated cash interest expense(2)	\$ 54.2
Actual interest coverage ratio(3)	2.64x
Minimum permitted interest coverage ratio	1.85x
<b>Calculation of maximum leverage ratio:</b>	
Simmons Company consolidated indebtedness	\$ 886.9
Less: 10% senior discount notes	192.0
Simmons Bedding consolidated indebtedness	694.9
Less: Simmons Bedding cash and cash equivalents	28.9
Simmons Bedding net debt	\$ 666.0
Simmons Bedding twelve months ended adjusted EBITDA(1)	\$ 143.2
Actual leverage ratio(4)	4.65x
Maximum permitted leverage ratio	6.25x

(1) Simmons Bedding's Adjusted EBITDA for the twelve months ended July 1, 2006 adds back to net income the following items: income taxes, interest expense, depreciation and amortization, non-cash stock compensation expense, transaction related expenditures, plant opening and closing charges, reorganization costs, management fees, state taxes in lieu of state income taxes and other non-recurring/non-cash charges as permitted under Simmons Bedding's senior credit facility.

(2) A calculation of Simmons Bedding's consolidated cash interest expense, as defined in its senior credit facility, for the twelve months ended July 1, 2006, as follows (in millions):

Simmons Company interest expense, net	\$ 80.5
Less: Simmons Company non-cash interest expense	(18.3)
Simmons Bedding interest expense, net	62.2
Add: Simmons Bedding interest income	0.4
Less: Call premium included in interest expense	(0.8)
Simmons Bedding gross interest expense	61.8
Less: Simmons Bedding non-cash interest expense	(7.6)
	\$ 54.2

(3) Represents ratio of Adjusted EBITDA to consolidated cash interest expense.

(4) Represents ratio of consolidated indebtedness less cash and cash equivalents to Adjusted EBITDA.

## Off-Balance Sheet Arrangements

In connection with the sale of Gallery Corp. to Pacific Coast Mattress, Inc. (PCM) on May 1, 2004, we continue to guarantee approximately \$0.6 million of PCM's obligations under certain store and warehouse leases that expire over various periods through 2010. We have no liability recorded for this obligation on our condensed consolidated balance sheet as of July 1, 2006.

## Seasonality/Other

Our third quarter sales are typically higher than sales for our other fiscal quarters. We attribute this seasonality principally to retailers' sales promotions related to the 4<sup>th</sup> of July and Labor Day holidays.

## Accounting Pronouncements

In February 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard ("SFAS") No. 155, *Accounting for Certain Hybrid Instruments* ("SFAS 155"). SFAS 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. SFAS 155 is effective for all financial instruments acquired or issued by us beginning in fiscal year 2007. We do not have any financial instruments that have embedded derivatives and do not expect this statement to have a significant impact on our consolidated financial statements or results of operations.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets - An Amendment of FASB Statement No. 140* ("SFAS 156"). Among other requirements, SFAS 156 provides guidance on the accounting for servicing assets or liabilities when an entity undertakes an obligation to service a financial asset by entering into a service contract. SFAS 156 is effective for us at the beginning of fiscal year 2007. We do not expect this statement to have a significant impact on our consolidated financial statements or results of operations.

In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for us at the beginning of fiscal year 2007. We are in the process of evaluating the impact of this guidance on our consolidated financial statements and our results of operations.

## Forward Looking Statements

“*Safe Harbor*” statement under the *Private Securities Litigation Reform Act of 1995*. When used in this Quarterly Report on Form 10-Q, the words “believes,” “anticipates,” “expects,” “intends,” “projects” and similar expressions are used to identify forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements relate to future financial and operating results, including expected benefits from our products. Any forward-looking statements contained in this report represent our management’s current expectations, based on present information and current assumptions, and are thus prospective and subject to risks and uncertainties, which could cause actual results to differ materially from those expressed in such forward-looking statements. Actual results could differ materially from those anticipated or projected due to a number of factors. These factors include, but are not limited to:

- . competitive pricing pressures in the bedding industry;
- . legal and regulatory requirements;
- . the success of our new products;
- . our relationships with and viability of our major suppliers;
- . fluctuations in costs of our raw materials;
- . our relationship with significant customers and licensees;
- . our ability to increase prices on our products and the effect of these price increases on our unit sales;
- . an increase in our return rates and warranty claims;
- . our labor relations;
- . departure of our key personnel;
- . encroachments on our intellectual property;
- . our product liability claims;
- . our level of indebtedness;
- . interest rate risks;
- . compliance with covenants in our debt agreements;

- our future acquisitions;
- our ability to achieve the expected benefits from any personnel realignments; and
- other risks and factors identified from time to time in the Company's reports filed with the Securities and Exchange Commission ("SEC").

All forward-looking statements attributable to us or persons acting on our behalf apply only as of the date of this Quarterly Report on Form 10-Q and are expressly qualified in their entirety by the cautionary statements included in this Quarterly Report on Form 10-Q. Except as may be required by law, we undertake no obligation to publicly update or revise forward-looking statements which may be made to reflect events or circumstances after the date made or to reflect the occurrence of unanticipated events.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Information relative to our market risk sensitive instruments by major category as of December 31, 2005 is presented under Item 7A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2005.

#### **Market Risk**

The principal market risks to which we are exposed that may adversely affect our results of operations and financial position include changes in future raw material prices and interest rates. We seek to minimize or manage these market risks through normal operating and financing activities and through the use of interest rate cap agreements, where practicable. We do not trade or use instruments with the objective of earning financial gains on the interest rate fluctuations, nor do we use instruments where there are not underlying exposures.

#### **Interest Rate Risk**

We are exposed to market risks from changes in interest rates. Simmons Bedding has developed and implemented a policy to utilize extended Eurodollar contracts to minimize the impact of near term Eurodollar rate increases. For \$258 million of the tranche D term loan, Simmons Bedding set the interest rate utilizing twelve month Eurodollar rate loans which fixed the Eurodollar Rate at 4.875% through January 26, 2007. The execution of this debt instrument resulted in Simmons Bedding fixing the interest rate on approximately 53% of its floating rate debt.

All other factors remaining unchanged, a hypothetical 10% increase or decrease in interest rates in effect on our floating rate debt as of July 1, 2006 would result in an additional \$0.5 million and \$4.4 million of interest expense in 2006 and 2007, respectively.

## **Commodity Price Risk**

The major raw materials that we purchase for production are foam, wire, spring components, lumber, cotton, insulator pads, innersprings, foundation constructions, fabrics and roll goods consisting of foam, fiber, ticking and non-wovens. The price and availability of these raw materials are subject to market conditions affecting supply and demand. In particular, many of our goods can be impacted by fluctuations in petrochemical and steel prices. For the first six months of 2006, the costs of our raw materials have been above historical price averages and we expect prices to remain at current levels or increase further for the remainder of 2006. Additionally, our distribution costs can be impacted by fluctuations in diesel prices. We currently do not have a hedging program in place to manage fluctuations in commodity prices.

## **Item 4. Internal Controls and Procedures**

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report (the "Evaluation Date"). Based on this evaluation, our principal executive officer and principal financial officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective such that the information relating to the Company, including our consolidated subsidiaries, required to be disclosed in our SEC reports (i) is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) is accumulated and communicated to the Company's management, including our principal executive and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

**PART II - OTHER INFORMATION**

**Item 1. Legal Proceedings**

See Note H to the Condensed Consolidated Financial Statements, Part 1, Item 1 included herein.

**Item 1A. Risk Factors**

There were no material changes to the Company's risk factors outlined in its annual report filed with the Commission on form 10-K on March 14, 2006.

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

None

**Item 3. Defaults Upon Senior Securities**

None

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

None

**Item 5. Other Information**

None

**Item 6. Exhibits**

- 10.1 Unit Purchase Agreement by and among ST San Diego, LLC, Sleep Country USA, Inc., SC Holdings, Inc. and Simmons Bedding Company
- 31.1 Chief Executive Officer Certification of the Type Described in Rule 13a - 14(a) and Rule 15d - 14(a)
- 31.2 Chief Financial Officer Certification of the Type Described in Rule 13a - 14(a) and Rule 15d - 14(a)
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 (furnished herewith)
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 (furnished herewith)

SIGNATURES

Pursuant to the requirements of the Securities Act of 1934, Simmons Company has duly caused this report to be signed on its behalf by the undersigned thereto duly authorized.

SIMMONS COMPANY

By: /s/ William S. Creekmuir

Name: William S. Creekmuir

Title: Executive Vice President & Chief Financial Officer

Date: August 15, 2006



## CERTIFICATIONS

## CHIEF EXECUTIVE OFFICER'S SECTION 302 CERTIFICATION

I, Charles R. Eitel, Chief Executive Officer of Simmons Company, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Simmons Company;
  2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
  3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
  4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
    - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
-

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 15, 2006

/s/ Charles R. Eitel

Name: Charles R. Eitel

Title: Chief Executive Officer

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## CHIEF FINANCIAL OFFICER'S SECTION 302 CERTIFICATION

I, William S. Creekmuir, Chief Financial Officer of Simmons Company, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Simmons Company;
  2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
  3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
  4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15 (e) and 15d-15(e)) for the registrant and have:
    - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    - (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    - (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
-

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 15, 2006

/s/ William S. Creekmuir  
Name: William S. Creekmuir  
Title: Chief Financial Officer

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CERTIFICATION REQUIRED BY 18 U.S.C. SECTION 1350  
(AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002)

I, Charles R. Eitel, as Chief Executive Officer of Simmons Company (the "Company"), certify, pursuant to 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002), that to my knowledge:

(1) the Quarterly Report on Form 10-Q of the Company for the quarter ended July 1, 2006 (the "Report"), being filed with the U.S. Securities and Exchange Commission on the date hereof, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 15, 2006

/s/ Charles R. Eitel

Name: Charles R. Eitel

Title: Chief Executive Officer

A signed original of this written statement required by Section 906 has been provided to Simmons Company and will be retained by Simmons Company and furnished to the Securities and Exchange Commission or its staff upon request.

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CERTIFICATION REQUIRED BY 18 U.S.C. SECTION 1350  
(AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002)

I, William S. Creekmuir, as Chief Financial Officer of Simmons Company (the "Company"), certify, pursuant to 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002), that to my knowledge:

(1) the Quarterly Report on Form 10-Q of the Company for the quarter ended July 1, 2006 (the "Report"), being filed with the U.S. Securities and Exchange Commission on the date hereof, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 15, 2006

/s/ William S. Creekmuir  
Name: William S. Creekmuir  
Title: Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Simmons Company and will be retained by Simmons Company and furnished to the Securities and Exchange Commission or its staff upon request.

UNIT PURCHASE AGREEMENT

BY AND AMONG

ST SAN DIEGO, LLC,

SLEEP COUNTRY USA, INC.,

SC HOLDINGS, INC.

AND

SIMMONS BEDDING COMPANY

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Dated as of July 24, 2006

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## UNIT PURCHASE AGREEMENT

This UNIT PURCHASE AGREEMENT (the "Agreement"), dated as of July 24, 2006, by and among ST San Diego, LLC, a California limited liability company ("Purchaser"), Sleep Country USA, Inc., a Delaware corporation, which immediately preceding the Closing (as defined below) shall be converted to a Delaware limited liability company (the "Company"), SC Holdings, Inc., a Delaware corporation ("Holdings"), and Simmons Bedding Company, a Delaware corporation ("Simmons").

### WITNESSETH:

WHEREAS, Holdings owns an aggregate of 3,000 shares of the Company's common stock, \$0.01 par value per share (the "Shares"), which constitute all of the issued and outstanding shares of capital stock of the Company;

WHEREAS, prior to the Closing, Holdings will convert the Company into a Delaware limited liability company named Sleep Country USA, LLC (the "Conversion"), and, after the effective time of the Conversion, the Company shall be deemed, for all purposes of and in accordance with the laws of the State of Delaware, to be the same entity as the Company prior to the Conversion;

WHEREAS, after the Conversion, Holdings will own 100 units of the Company's common units (the "Units"), which Units will constitute, immediately prior to Closing, all of the issued and outstanding equity interests of the Company;

WHEREAS, Holdings desires to sell to Purchaser, and Purchaser desires to purchase from Holdings, the Units for the purchase price and upon the terms and conditions hereinafter set forth; and

WHEREAS, Simmons owns 100% of the issued and outstanding shares of capital stock of Holdings and will receive substantial benefits from the transactions contemplated hereby.

NOW, THEREFORE, in consideration of the premises and the mutual covenants and agreements hereinafter contained, the parties hereby agree as follows:

## ARTICLE I

### DEFINITIONS

#### 1.1 Certain Definitions.

(a) For purposes of this Agreement, the following terms shall have the meanings specified in this Section 1.1:

"Actual Knowledge" means the actual knowledge of Steve Fendrich, Joe Paviglianti, Terry Horsley, Richard Thomas, Charles Dieteker, Jacqueline Steven, Bill Creekmuir or Kristen McGuffey, or any knowledge which would have been obtained by any such person after inquiry of such other named persons, but without any other inquiry.

"Adjusted EBITDA" has the meaning specified on Schedule 1 attached hereto.

"Affiliate" means, with respect to any Person, any other Person that, directly or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, such Person, and the term "control" (including the terms "controlled by" and "under common control with") means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of such Person, whether through ownership of voting securities, by contract or otherwise.

"Business Day" means any day of the year on which national banking institutions in California and Georgia are open to the public for conducting business and are not required or authorized to close.

"Closing Date Debt" means, without duplication, (A) the amount of (i) the aggregate debt for borrowed money (excluding current liabilities) of the Company outstanding on the Closing Date, and (ii) any amount, whether or not a current liability, owed by the Company to Simmons, Dreamwell, Ltd., a Nevada limited liability company, or any of their respective Affiliates (excluding trade payables incurred in the Ordinary Course of Business), all of which will be required to be repaid by the Company at or immediately prior to the Closing Date, and all prepayment penalties and costs incurred or to be incurred by the Company (or Purchaser) in connection therewith, and (B) the aggregate payoff amount reflected in payoff letters provided on or before the Closing Date in respect of any capitalized equipment lease obligations of the Company (or, if payoff letters are not so provided in respect of any capitalized equipment lease obligations, the aggregate amount of the present value under any such obligations as of the Closing Date determined in accordance with the historical accounting practices of the Company).

"Code" means the Internal Revenue Code of 1986, as amended.

"Contract" means any written or oral contract, agreement, indenture, note, bond, mortgage, loan, instrument, lease, license, restriction, understanding or undertaking of any kind or character.

"Environmental Law" means any applicable Law currently in effect relating to the protection of the environment or natural resources, including the Comprehensive Environmental Response, Compensation and Liability Act (42 U.S.C. § 9601 et seq.), the Hazardous Materials Transportation Act (49 U.S.C. App. § 1801 et seq.), the Resource Conservation and Recovery Act (42 U.S.C. § 6901 et seq.), the Clean Water Act (33 U.S.C. § 1251 et seq.), the Clean Air Act (42 U.S.C. § 7401 et seq.), the Toxic Substances Control Act (15 U.S.C. § 2601 et seq.), and the Federal Insecticide, Fungicide, and Rodenticide Act (7 U.S.C. § 136 et seq.), as each has been amended and the regulations promulgated pursuant thereto.

"Excess Cash" means the amount of any and all cash and cash equivalents of the Company (excluding Petty Cash) as of the Closing Date equal to the excess of current assets of the Company (excluding Petty Cash) over current liabilities of the Company as of the Closing Date, as determined in accordance with GAAP.

“Force Majeure Event” means acts of god or the public enemy, fire, flood, earthquake, war, military action or hostilities, terrorism, sabotage or similar events.

“GAAP” means generally accepted accounting principles in the United States, consistently applied in accordance with the Company’s historical practice.

“Governmental Body” means any government or governmental or regulatory body thereof, or political subdivision thereof, whether federal, state, local or foreign, or any agency, instrumentality or authority thereof, or any court or arbitrator (public or private).

“Hazardous Material” means any substance, material or waste which is regulated by any Governmental Body including petroleum and its by-products, asbestos, and any material or substance which is defined as a “hazardous waste,” “hazardous substance,” “hazardous material,” “restricted hazardous waste,” “industrial waste,” “solid waste,” “contaminant,” “pollutant,” “toxic waste” or “toxic substance” under any provision of Environmental Law.

“HSR Act” means the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended and the rules and regulations promulgated thereunder.

“Intellectual Property” means all intellectual property rights owned or used by the Company arising from or in respect of the following: (i) patents and patent applications, including continuations, divisionals, continuations-in-part, reissues or reexaminations and patents issuing thereon (collectively, “Patents”), (ii) trademarks, service marks, trade dress, logos, corporate names, trade names and Internet domain names, together with the goodwill associated with any of the foregoing, and all applications and registrations therefor (collectively, “Marks”), (iii) copyrights and registrations and applications therefor, works of authorship and moral rights (collectively, “Copyrights”), (iv) confidential and proprietary information, including trade secrets, discoveries, concepts, ideas, research and development, algorithms, know-how, formulae, inventions (whether or not patentable), processes, techniques, technical data, designs, drawings, specifications, databases, and customer lists, in each case excluding any rights in respect of any of the foregoing that comprise or are protected by Patents (collectively, “Trade Secrets”) and (v) Software.

“IRS” means the United States Internal Revenue Service and, to the extent relevant, the United States Department of Treasury.

“Knowledge of the Company” means the actual knowledge of Steve Fendrich, Joe Paviglianti, Terry Horsley, Richard Thomas, Charles Dieteker, Jacqueline Steven, Bill Creekmuir or Kristen McGuffey, or any knowledge which would have been obtained by any such person after inquiry that a reasonably prudent person would undertake in the particular circumstance.

“Knowledge of the Purchaser” means the actual knowledge of Dale Carlsen, Michael Dunn, Kevin Moreton, Robert Killgore, Michael Combest, John Haitz, Paul Grimm or Bruce Kerr, or any knowledge which would have been obtained by any such person after inquiry that a reasonably prudent person would undertake in the particular circumstance.

“Law” means any foreign, federal, state, local law, statute, code, ordinance, rule or regulation, or any decree, injunction, judgment, order or ruling.

“Legal Proceeding” means any judicial, administrative or arbitral actions, suits or proceedings (public or private) by or before a Governmental Body.

“Liability” means any debt, liability or obligation (whether known or unknown, direct or indirect, absolute or contingent, accrued or unaccrued, liquidated or unliquidated, or due or to become due and whether or not required to be reflected or reserved against on a balance sheet under GAAP) and including all costs and expenses relating thereto.

“Lien” means any lien, encumbrance, pledge, mortgage, deed of trust, security interest, lease, charge, option, right of first refusal, easement, servitude, transfer restriction, or adverse claim or right of any kind or character.

“Material Adverse Effect” means any circumstance, occurrence of any event, change in, or effect on the Company that, individually or when taken with all other related circumstances, events, changes in or effects on the Company, has (or is reasonably likely to have) a materially adverse effect (financial or otherwise) on (i) the business, assets, properties, results of operations or financial condition of the Company or (ii) the ability of the Company to consummate the transactions contemplated by this Agreement, other than an effect resulting from an Excluded Matter. “Excluded Matter” means any one of the following: (i) the effect of any change in the United States economy or securities or financial markets in general, which change does not disproportionately affect the Company and which is not the result of a Force Majeure Event; (ii) the effect of any change that generally affects any industry in which the Company operates, which such change does not disproportionately affect the Company and which is not the result of a Force Majeure Event; (iii) the effect of any action taken by Purchaser or its Affiliates with respect to the transactions contemplated hereby or with respect to the Company; or (iv) any effect resulting from the public announcement of this Agreement, compliance with terms of this Agreement or the consummation of the transactions contemplated by this Agreement.

“Order” means any order, injunction, judgment, decree, ruling, writ, assessment or arbitration award of a Governmental Body.

“Ordinary Course of Business” means solely any act or omission that (i) is in the ordinary and usual course of normal day-to-day operations of the Company, consistent with historical practices, (ii) does not relate to any breach of Contract, tort, infringement, willful misconduct or violation of Law, and (iii) does not require, under Law, Contract or consistent with the historical practices of the Company, authorization by the Company’s Board of Directors.

“Permits” means any approvals, authorizations, consents, licenses, permits or certificates of a Governmental Body.

“Permitted Exceptions” means (i) all defects, exceptions, restrictions, easements, rights of way and encumbrances disclosed in policies of title insurance and on Schedule 5.10(a); (ii) statutory liens for current Taxes, assessments or other governmental charges not yet due or the amount or validity of which is being contested in good faith by appropriate proceedings; (iii) zoning, entitlement and other land use and environmental regulations by any Governmental Body; (iv) title of a lessor under a capital or operating lease or any Real Property Lease, together with any defects, easements, restrictions, exceptions, rights of way and encumbrances to which any such lessor is subject; and (v) such other imperfections in title, charges, easements, restrictions and encumbrances not arising out of or relating to the failure of the Company to pay any amount when due which would not result in Losses or Liabilities to the Company in excess of \$10,000.

“Person” means any individual, corporation, partnership, limited liability company, firm, joint venture, association, joint-stock company, trust, unincorporated organization, Governmental Body or other entity.

“Petty Cash” means the amount of petty cash kept on hand at each of the Company’s stores, distribution centers, corporate offices and other facilities and excluding cash in bank accounts or uncashed checks, all in the Ordinary Course of Business.

“Release” means any release, spill, emission, leaking, pumping, injection, deposit, disposal, discharge, dispersal, or leaching into the environment.

“Remedial Action” means all actions required under Environmental Laws to clean up, remove, treat or address any Hazardous Material in the environment at levels exceeding those allowed by applicable Environmental Laws, including pre-remedial studies and investigations or post-remedial monitoring and care.

“Senior Executives” means the following individuals: Joe Paviglianti, Terry Horsley, Richard Thomas, Charles Dieteker, Jacqueline Steven and, for 2005, Steven Fendrich.

“Software” means any and all (i) computer programs, including any and all software implementations of algorithms, models and methodologies, whether in source code or object code, and (ii) databases and compilations, including any and all data and collections of data, whether machine readable or otherwise.

“Subsidiary” means any Person of which a majority of the outstanding share capital, voting securities or other voting equity interests are owned, directly or indirectly, by the Company.

“Tax” or “Taxes” means (i) all federal, state, local or foreign taxes, charges, fees, imposts, levies or other assessments, including all net income, gross receipts, capital, sales, use, ad valorem, value added, transfer, franchise, profits, inventory, capital stock, license, withholding, payroll, employment, social security, unemployment, excise, severance, stamp, occupation, property and estimated taxes, customs duties, fees, assessments and charges of any kind whatsoever, and (ii) all interest, penalties, fines, additions to tax or additional amounts imposed by any Taxing Authority in connection with any item described in clause (i).

“Taxing Authority” means the IRS and any other Governmental Body responsible for the administration of any Tax.

“Tax Return” means any return, report or statement required to be filed with respect to any Tax (including any attachments thereto, and any amendment thereof), including any information return, claim for refund, amended return or declaration of estimated Tax, and including, where permitted or required, com-bined, consolidated or unitary returns for any group of entities that includes Holdings or any of their Affiliates.

“Technology” means, collectively, all information, designs, formulae, algorithms, procedures, methods, techniques, ideas, know-how, research and development, technical data, programs, subroutines, tools, materials, specifications, processes, inventions (whether patentable or unpatentable and whether or not reduced to practice), apparatus, creations, improvements, works of authorship and other similar materials, and all recordings, graphs, drawings, reports, analyses, and other writings, and other tangible embodiments of the foregoing, in any form whether or not specifically listed herein, and all related technology, that are used in, incorporated in, embodied in, displayed by or relate to, or are used by the Company.

“WARN Act” means the Worker Adjustment and Retraining Notification Act of 1988, as amended, and the rules and regulations promulgated thereunder.

“Working Capital” means the current assets (excluding Petty Cash and deferred tax benefits) of the Company, reduced by the current liabilities of the Company (including any intercompany Liabilities owed to Simmons, Dreamwell, Ltd. and their Affiliates (other than the Company), in each case determined in accordance with GAAP. Items already included in Closing Date Debt shall not be included in Working Capital.

1.2 Terms Defined Elsewhere in this Agreement. For purposes of this Agreement, the following terms have meanings set forth in the sections indicated:

<u>Term</u>	<u>Section</u>
Actual Closing Date Working Capital	3.3(a)
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### 1.3 Other Definitional and Interpretive Matters.

- (a) Unless otherwise expressly provided, for purposes of this Agreement, the following rules of interpretation shall apply:

Calculation of Time Period. When calculating the period of time before which, within which or following which any act is to be done or step taken pursuant to this Agreement, the date that is the reference date in calculating such period shall be excluded. If the last day of such period is a non-Business Day, the period in question shall end on the next succeeding Business Day. Notwithstanding the foregoing, for purposes of any calculation used herein referring to July 1, 2006, the calculation date shall be July 1, 2006, notwithstanding the fact it is a Saturday.

Dollars. Any reference in this Agreement to \$ shall mean U.S. dollars.

Exhibits/Schedules. The Exhibits and Schedules to this Agreement are hereby incorporated and made a part hereof and are an integral part of this Agreement. All Exhibits and Schedules annexed hereto or referred to herein are hereby incorporated in and made a part of this Agreement as if set forth in full herein. Any matter or item disclosed on one Schedule shall be deemed to have been disclosed on each other Schedule, to the extent reasonably apparent on its face. Disclosure of any item on any Schedule shall not constitute an admission or indication that such item or matter is material or would have a Material Adverse Effect. No disclosure on a Schedule relating to a possible breach or violation of any Contract, Law or Order shall be construed as an admission or indication that breach or violation exists or has actually occurred. Any capitalized terms used in any Schedule or Exhibit but not otherwise defined therein shall be defined as set forth in this Agreement.

Gender and Number. Any reference in this Agreement to gender shall include all genders, and words imparting the singular number only shall include the plural and vice versa.

Headings. The provision of a Table of Contents, the division of this Agreement into Articles, Sections and other subdivisions and the insertion of headings are for convenience of reference only and shall not affect or be utilized in construing or interpreting this Agreement. All references in this Agreement to any "Section" are to the corresponding Section of this Agreement unless otherwise specified.

Herein. The words such as "herein," "hereinafter," "hereof," and "hereunder" refer to this Agreement as a whole and not merely to a subdivision in which such words appear unless the context otherwise requires.

Including. The word "including" or any variation thereof means (unless the context of its usage otherwise requires) "including, without limitation" and shall not be construed to limit any general statement that it follows to the specific or similar items or matters immediately following it.

Reflected On or Set Forth In. An item arising with respect to a specific representation or warranty shall be deemed to be "reflected on" or "set forth in" a balance sheet or financial statements, to the extent any such phrase appears in such representation or warranty, if (a) there is a reserve, accrual or other similar item underlying a number on such balance sheet or financial statements that related to the subject matter of such representation, (b) such item is otherwise specifically set forth on the balance sheet or financial statements or (c) such item is reflected on the balance sheet or financial statements and is specifically set forth in the notes thereto.

- (b) The parties hereto have participated jointly in the negotiation and drafting of this Agreement and, in the event an ambiguity or question of intent or

interpretation arises, this Agreement shall be construed as jointly drafted by the parties hereto and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any provision of this Agreement.

## ARTICLE II

### SALE AND PURCHASE OF UNITS

2.1 Sale and Purchase of Units. Upon the terms and subject to the conditions contained herein, on the Closing Date, Holdings agrees to sell to Purchaser, and Purchaser agrees to purchase from Holdings, the Units.

2.2 Allocation of Purchase Price. The sale of the Units shall be treated as a sale of assets of the Company for federal, state and local income Tax purposes. At Closing, Simmons and Purchaser shall agree upon a good faith allocation of the Purchase Price and any other items that are treated as additional purchase price for federal, state and local income Tax purposes among the different items of assets of the Company and the covenant described in Section 8.11 and attach hereto as Schedule 2 a statement (the "Allocation Statement") evidencing such allocation. Purchaser shall provide to Simmons from time to time revised copies of the Allocation Statement (the "Revised Statements") so as to report any matter on the Allocation Statement that needs updating (including Purchase Price adjustments, if any). Simmons shall have 20 days to review the last Revised Statements and will notify Purchaser of disputes with any revised allocation. The parties shall act in good faith to resolve any such dispute. If the parties cannot resolve the disputed allocation then the Arbiter (as defined herein) shall review and determine the proper allocation. This allocation will be binding on the parties. Any Arbiter fees and expenses shall be borne one-half by Purchaser and one-half by Simmons.

## ARTICLE III

### PURCHASE PRICE

3.1 Purchase Price. The aggregate consideration for the Units shall be an amount in cash equal to (i) 6.0 times the Adjusted EBITDA for the last full 12-month period ended on July 1, 2006, minus (ii) any Closing Date Debt, minus (iii) any amount by which Estimated Closing Date Working Capital is less than zero, plus (iv) any amount by which the Estimated Closing Date Working Capital exceeds zero, minus (v) the amount, if any, by which the aggregate rebates, co-op advertising and return allowances as of the Closing Date (collectively, the "Incentives") exceeds the aggregate receivables relating to Incentives as of the Closing Date, plus (vi) the amount, if any, by which the aggregate receivables relating to Incentives as of the Closing Date exceeds the amount of the Incentives (the "Purchase Price"). Any Excess Cash will be distributed by the Company to Holdings immediately prior to Closing (after calculation of the Estimated Closing Date Working Capital), and all Petty Cash will be retained by the Company.

3.2 Calculation and Payment of Purchase Price. Attached as Schedule 3 hereto is a statement agreed to by the parties estimating as of July 1, 2006 (as if the Closing had occurred as of the end of business on such date) the items set forth in items (i) - (vi) of this Section 3.2 below (the "Preliminary Statement"). At least 5 Business Days prior to the Closing Date, the Company shall deliver to Purchaser: (i) a calculation of Adjusted EBITDA; (ii) a calculation of the estimated Working Capital of the Company as of the Closing Date (prior to the distribution of any Excess Cash) determined in accordance with GAAP (the "Estimated Closing Date Working Capital") and reflected in a statement in substantially the form attached hereto as Exhibit A and in accordance with the methodology used in Schedule 3 hereto (the "Estimated Closing Date Working Capital Statement"); (iii) a calculation of the Closing Date Debt (together with customary pay-off letters from all holders of Closing Date Debt to be repaid as of or prior to the Closing); (iv) a calculation of Excess Cash and Petty Cash; (v) a calculation of the amounts under Section 3.1 (iv) and (v) above; and (vi) a calculation of the Purchase Price to be paid at Closing. Such calculations and statements provided by the Company shall be subject to the review and approval of Purchaser. On the Closing Date, Purchaser shall pay the Purchase Price to Holdings, which shall be paid by wire transfer of immediately available United States funds into an account designated by Holdings.

3.3 Post-Closing Purchase Price Adjustment. Following the Closing, the Purchase Price shall be adjusted as provided in this Section 3.3 to reflect any difference between the Actual Closing Date Working Capital and the Estimated Closing Date Working Capital.

(a) Within 60 days following the Closing Date, Purchaser shall deliver to Simmons a calculation of the actual Working Capital of the Company as of the Closing Date (prior to the distribution of any Excess Cash) determined in accordance with GAAP (the "Actual Closing Date Working Capital") and reflected in a statement substantially in the form of Exhibit A attached hereto (the "Actual Closing Date Working Capital Statement").

(b) Acceptance of Statements; Dispute Procedures. The Actual Closing Date Working Capital Statement delivered by Purchaser to Simmons shall be conclusive and binding upon the parties unless Simmons, within 20 Business days after delivery to Simmons of the Actual Closing Date Working Capital Statement, notifies Purchaser in writing that Simmons disputes any of the amounts set forth therein, specifying the nature of the dispute and the basis therefor. Purchaser shall grant Holdings, Simmons and their Affiliates and representatives (including advisors and accountants) access to all books, records and employees of the Company that is reasonably requested by Holdings or Simmons in connection with Purchaser's preparation of the Actual Closing Date Working Capital Statement. The parties shall in good faith attempt to resolve any dispute and, if the parties so resolve all disputes, the Actual Closing Date Working Capital Statement, as amended to the extent necessary to reflect the resolution of the dispute, shall be conclusive and binding on the parties. If the parties do not reach agreement in resolving the dispute within 15 days after notice is given by Simmons to Purchaser pursuant to the second preceding sentence, the parties shall submit the dispute to Deloitte & Touche or such other nationally recognized independent accounting firm which is mutually agreeable to the parties (the "Arbiter") for resolution. Promptly, but no later than 20 days after acceptance of its appointment as Arbiter, the Arbiter shall determine (it being understood that in making such determination, the Arbiter shall be functioning as an expert and not as an arbitrator), based solely on written submissions by Purchaser and Simmons, and not by independent review, only those issues in dispute and shall render a written report as to the resolution of the dispute and the resulting computation of the Actual Closing Date Working Capital which shall be conclusive and binding on the parties. In resolving any disputed item, the Arbiter (x) shall be bound by the provisions of this Section 3.3 and (y) may not assign a value to any item greater than the greatest value for such items claimed by either party or less than the smallest value for such items claimed by either party. The fees, costs and expenses of the Arbiter shall be allocated to and borne equally by Purchaser and Simmons.

(c) Payment. Upon final determination of Actual Closing Date Working Capital as provided in Section 3.3(b) above, (A) if Actual Closing Date Working Capital is greater than Estimated Closing Date Working Capital, the Purchase Price shall be increased by the excess of the Actual Closing Date Working Capital over Estimated Closing Date Working Capital and Purchaser shall promptly, but no later than five Business Days after such final determination, pay the amount of such difference, together with interest thereon from the Closing Date to the date of payment thereof, to be distributed to Holdings, and (B) if Actual Closing Date Working Capital is less than Estimated Closing Date Working Capital, the Purchase Price shall be decreased by the excess of Estimated Closing Date Working Capital over Actual Closing Date Working Capital and Simmons shall promptly, but no later than five Business Days after such final determination, pay to Purchaser the amount of such difference, together with interest thereon from the Closing Date to

the date of payment thereof as determined below.

(d) Interest. For the purposes of Section 3.3(c), interest will be payable at the “prime” rate, as announced by the Wall Street Journal, Eastern Edition, as of the Closing Date, calculated based on a 365 day year and the actual number of days elapsed.

#### ARTICLE IV

##### CLOSING AND TERMINATION

4.1 Closing Date. The closing of the sale and purchase of the Units provided for in Section 2.1 hereof (the “Closing”) shall take place at the offices of Shartsis Friese LLP, One Maritime Plaza, 18<sup>th</sup> Floor, San Francisco, California 94111 (or at such other place as the parties may designate in writing) at 10:00 a.m. (San Francisco time) on a date to be specified by the parties (the “Closing Date”), which date shall be no later than the second Business Day after the satisfaction or waiver of the conditions set forth in Article IX (other than conditions that by their nature are to be satisfied at the Closing, but subject to the satisfaction or waiver of those conditions at such time), but in no event later than August 28, 2006, unless another time, date or place is agreed to in writing by the parties hereto. At the election of any party hereto, the Closing may take place through an exchange of consideration and documents using overnight courier service or facsimile.

4.2 Termination of Agreement. This Agreement may be terminated prior to the Closing as follows:

(a) At the election of Holdings or Purchaser on or after August 15, 2006, (the “Termination Date”), if the Closing shall not have occurred by the close of business on such date, provided that the terminating party is not in breach in any material respect of any of its covenants hereunder. Notwithstanding the foregoing, (i) the Termination Date shall be extended to August 28, 2006 if the only reason the Closing shall not have occurred by such date is due to either the waiting period applicable to the transactions contemplated by this Agreement under the HSR Act shall not have expired or early termination shall not have been granted (provided that the parties have complied with their obligations under Section 8.4 hereof); and (ii) the Termination Date shall be extended to August 22, 2006 if the only reason the Closing shall not have occurred by such date is due to the fact the condition set forth in Section 9.1(f) (consents) has not been met, but the Termination Date shall not be extended beyond August 28, 2006 without the consent of Simmons and Purchaser.

(b) by mutual written consent of Holdings and Purchaser;

(c) by Purchaser if Purchaser is not then in material breach of its obligations under this Agreement and there has been a material breach of any representation, warranty, covenant or agreement contained in this Agreement on the part of Company, Simmons or Holdings which has or would prevent one of the conditions set forth in section 9.1(a) or (b) from being satisfied, and Company, Simmons or Holdings, as the case may be, has not cured such breach within 15 days after notice thereof by Purchaser;

(d) by Company, Simmons or Holdings if none of Company, Simmons or Holdings is then in material breach of its obligations under this Agreement and there has been a material breach of any representation, warranty, covenant or agreement contained in this Agreement on the part of Purchaser which has or would prevent one of the conditions set forth in section 9.2(a) or (b) from being satisfied, and Purchaser has not cured such breach within 15 days after notice thereof by Company, Simmons or Holdings; or

(e) by Holdings or Purchaser if there shall be in effect a final nonappealable Order of a Governmental Body of competent jurisdiction restraining, enjoining or otherwise prohibiting the consummation of the transactions contemplated hereby; provided, however, that the right to terminate this Agreement under this Section 4.2(c) shall not be available to a party if such Order was primarily due to the failure of such party to perform any of its obligations under this Agreement.

4.3 Procedure Upon Termination. In the event of termination and abandonment by Purchaser or Holdings, or both, pursuant to Section 4.2 hereof, written notice thereof shall forthwith be given to the other party or parties, and this Agreement shall terminate, and the purchase of the Units hereunder shall be abandoned, without further action by Purchaser or Holdings.

4.4 Effect of Termination.

(a) In the event that this Agreement is validly terminated in accordance with Section 4.2 and 4.3, then each of the parties shall be relieved of their duties and obligations arising under this Agreement after the date of such termination and such termination shall be without liability to Purchaser, Simmons, the Company or Holdings; provided, however that no such termination shall relieve any party hereto from liability for any willful breach of this Agreement and, provided, further, that the obligations of the parties set forth in Section 8.6 and Article XI hereof shall survive any such termination and shall be enforceable hereunder.

(b) Nothing in this Section 4.4 shall relieve Simmons, Holdings, the Company or Purchaser of any liability for a breach of any of its covenants or agreements or willful breach of its representations and warranties contained in this Agreement prior to the date of termination. The damages recoverable by the non-breaching party shall include all attorneys’ fees reasonably incurred by such party in connection with the transactions contemplated hereby.

#### ARTICLE V

##### REPRESENTATIONS AND WARRANTIES REGARDING THE COMPANY

Simmons and Holdings hereby represent and warrant to Purchaser that:

5.1 Organization and Good Standing. The Company is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and has all requisite corporate power and authority to own, lease and operate its properties and to carry on its business as now conducted. The Company is duly qualified or authorized to do business and is in good standing under the laws of each jurisdiction in which it owns or leases real property and each other jurisdiction in which the conduct of its business or the ownership of its properties requires such qualification or authorization, except where the failure to be so qualified, authorized or in good standing would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate.

5.2 Authorization of Agreement. The Company has all requisite power and authority to execute and deliver this Agreement and each other agreement, document, or instrument or certificate contemplated by this Agreement or to be executed by the Company in connection with the consummation of the transactions contemplated by this

Agreement (the “Company Documents”), and to consummate the transactions contemplated hereby. The execution and delivery of this Agreement and the Company Documents and the consummation of the transactions contemplated hereby and thereby have been duly authorized by all requisite corporate action on the part of the Company. This Agreement has been, and each of the Company Documents will be at or prior to the Closing, duly and validly executed and delivered by the Company and (assuming the due authorization, execution and delivery by the other parties hereto and thereto) this Agreement constitutes the legal, valid and binding obligations of the Company, enforceable against it in accordance with its terms, subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors’ rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity).

### 5.3 Conflicts; Consents of Third Parties.

(a) Except as set forth on Schedule 5.3(a), none of the execution and delivery by the Company of this Agreement or the Company Documents, the consummation of the transactions contemplated hereby or thereby, or compliance by the Company with any of the provisions hereof or thereof will conflict with, or result in any violation of or default (with or without notice or lapse of time, or both) under, or give rise to a right of termination or cancellation under, any provision of (i) the certificate of incorporation and by-laws or comparable organizational documents of the Company; (ii) any Material Contract or Permit to which the Company is a party or by which any of the properties or assets of the Company are bound; (iii) any Order of any Governmental Body applicable to the Company or by which any of the properties or assets of the Company are bound; or (iv) any applicable Law, other than, in the case of Permits or clause (iv), such conflicts or violations that would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate.

(b) Except as set forth on Schedule 5.3(b), no consent, waiver, approval, Order, Permit or authorization of, or declaration or filing with, or notification to, any Person or Governmental Body is required on the part of the Company in connection with the execution and delivery of this Agreement or the Company Documents or the compliance by the Company with any of the provisions hereof or thereof, or the consummation of the transactions contemplated hereby or thereby, except for compliance with the applicable requirements of the HSR Act. The consents obtained by the Company prior to Closing are sufficient to enable the Purchaser to operate the business immediately following Closing in all material respects as it was operated prior to Closing.

### 5.4 Capitalization.

(a) The authorized capital stock of the Company as of the date hereof consists of 3,000 shares of common stock, \$0.01 par value per share (“Common Stock”). As of the date hereof, there are 3,000 shares of Common Stock issued and outstanding and no shares of Common Stock are held by the Company as treasury stock. All of the issued and outstanding Common Stock were duly authorized for issuance and are validly issued, fully paid and non-assessable and were not issued in violation of any purchase or call option, right of first refusal, subscription right, preemptive right or any similar rights. Except as set forth on Schedule 5.4(a), all of the Shares are free and clear of all Liens and claims of every kind.

(b) Except as set forth on Schedule 5.4(b), there is no existing option, warrant, call, right, or Contract of any character to which the Company is a party requiring, and there are no securities of the Company outstanding which upon conversion or exchange would require, the issuance, of any equity interests of the Company or other securities convertible into, exchangeable for or evidencing the right to subscribe for or purchase equity interests of the Company. The Company is not a party to any voting trust or other Contract with respect to the voting, redemption, sale, transfer or other disposition of the Common Stock of the Company.

(c) Except as set forth on Schedule 5.4(c), the Company has not authorized or issued debt securities or other instruments of indebtedness.

### 5.5 Subsidiaries. The Company has no Subsidiaries. The Company does not own, directly or indirectly, any capital stock or equity securities of any Person.

5.6 Financial Statements. The Company has made available to Purchaser copies of (i) the audited consolidated balance sheet of the Company as at December 28, 2002 and the related audited consolidated statement of income and of cash flows of the Company for the year then ended (such audited statements, including the related notes and schedules thereto, complete and correct copies of which are attached as Schedule 5.6, are referred to herein as the “Audited Financial Statements”), (ii) the unaudited consolidated balance sheets of the Company as at December 27, 2003, December 25, 2004 and December 31, 2005 and the related unaudited consolidated statements of income and cash flows of the Company for the years then ended (complete and correct copies of which are attached as Schedule 5.6), and (iii) the unaudited consolidated balance sheet of the Company as at June 3, 2006 and the related unaudited consolidated statement of income and cash flows of the Company for the five (5) month period then ended (such unaudited statements, including the related notes and schedules thereto, complete and correct copies of which are attached as Schedule 5.6, are referred to herein as the “Unaudited Financial Statements”). Except as set forth in the notes thereto and as disclosed in Schedule 5.6, each of the Audited Financial Statements has been prepared in accordance with GAAP and presents fairly in all material respects the financial position, results of operations and cash flows of the Company as at the dates and for the periods indicated therein. Except as set forth in the notes thereto and as disclosed in Schedule 5.6, each of the Unaudited Financial Statements has been prepared in accordance with the historical accounting practices of the Company and presents fairly in all material respects the financial position, results of operations and cash flows of the Company as at the dates and for the periods indicated therein.

For the purposes hereof, the unaudited balance sheet of the Company as at June 3, 2006 is referred to as the “Balance Sheet” and June 3, 2006 is referred to as the “Balance Sheet Date”.

5.7 No Undisclosed Liabilities. The Company does not have any Liabilities of any kind that would have been required to be reflected in, reserved against or otherwise described on the Balance Sheet or in the notes thereto in accordance with GAAP and were not so reflected, reserved against or described, other than (i) Liabilities incurred in the Ordinary Course of Business after the Balance Sheet Date, (ii) Liabilities incurred in connection with the transactions contemplated hereby and (iii) Liabilities that would not be in excess of \$75,000 individually or \$150,000 in the aggregate.

5.8 Absence of Certain Developments. Except as set forth on Schedule 5.8, since the Balance Sheet Date, the business has been conducted only in the Ordinary Course of Business and there has not been:

(a) any change in its financial condition, assets, liabilities (contingent or otherwise), income, operations or business which would have an effect on the financial condition, assets, liabilities (contingent or otherwise), income, operations of the Company or the business, taken as a whole, resulting in Losses in excess of \$75,000 individually or \$150,000 in the aggregate;

(b) any damage, destruction or loss (whether or not covered by insurance) adversely affecting any material portion of its properties or business;

(c) any capital expenditure or commitment by the Company in excess of \$75,000 individually or \$150,000 in the aggregate;

(d) any unfair labor practices or charges, strikes, work stoppages, slowdowns or lockouts or labor grievance or complaints that would reasonably be expected to result in Losses in excess of \$75,000 individually or \$150,000;

(e) any plan, agreement or arrangement granting any preferential rights to purchase or acquire any interest in any of its assets, property or rights or requiring consent of any part to the transfer and assignment of any such assets, property or rights;

(f) any new or any amendment or termination of any existing Material Contract to which it is a party; or

(g) any action or event that, if it occurred after the date of this Agreement, would have required the consent of Purchaser under Section 8.2.

5.9 Taxes. Except as set forth on Schedule 5.9:

(a) All income Tax and other material Tax Returns required to be filed by the Company have been properly completed and filed on a timely basis or otherwise properly extended for subsequent filing by the authorized due dates. The foregoing Tax Returns are correct in all material respects. No extension of time within which to file any income Tax or other material Tax Return of the Company is outstanding.

(b) With respect to all taxable periods or portions of periods ending on or prior to Closing, all material amounts of Taxes required to be paid by the Company (whether or not required to be shown on any Tax Return and whether or not any Tax Return was required) have been paid.

(c) No material issues have been raised (and are currently pending) in writing in respect of the Company by any Taxing Authority in connection with any of its Tax Returns. As of the date hereof, no waivers of statutes of limitation with respect to any of the Tax Returns described in clause (a) above have been given by or requested from the Company. All material deficiencies asserted or assessments made as a result of any examinations have been fully paid, or are fully reflected as a liability in the Audited Financial Statements in accordance with GAAP or the Unaudited Financial Statements in accordance with the historical accounting practices of the Company, as the case may be. There are no Liens on any of the assets of the Company that arose in connection with any failure or alleged failure to pay any Tax, except for Permitted Exceptions.

(d) The Company has withheld and paid all material Taxes required to have been withheld and paid in connection with amounts paid or owing to any employee, independent contractor, creditor, stockholder or other third party.

(e) Except for the affiliated group of which Simmons is the ultimate parent, since February 1, 2003, the Company has not been a member of an affiliated group of corporations, within the meaning of Section 1504 of the Code.

(f) The Company is not a party to and has no obligation under any Tax sharing, Tax indemnity or Tax allocation agreement or arrangement (other than such agreements existing as of the date hereof between current members of the Company's affiliated group and customary Tax indemnification contained in credit or other commercial agreements, the primary purpose of which does not relate to Taxes).

(g) To the Knowledge of the Company, none of the Company's assets are tax-exempt use property within the meaning of Section 168(h) of the Code.

(h) The Company has not with respect to any open taxable period applied for and been granted permission to adopt a change in its method of Tax accounting requiring adjustments under Section 481 of the Code or comparable state or foreign Law.

(i) During the two-year period ending on the Closing Date, the Company was not a distributing corporation or a controlled corporation in a transaction intended to be governed by Section 355 of the Code.

(j) No payment made to any employee, officer, director or independent contractor of the Company (the "Recipient") pursuant to any employment contract, severance agreement or other arrangement (a "Golden Parachute Payment") will be nondeductible by the Company because of the application of Sections 280G and 4999 of the Code to any Golden Parachute Payment, nor will the Company be required to compensate any Recipient because of the imposition of an excise tax (including any interest or penalties related thereto) on the Recipient by reason of Sections 280G and 4999 of the Code.

(k) This Section 5.9 represents the sole and exclusive representations and warranties of Simmons and Holdings with respect to Tax matters of the Company.

5.10 Real Property.

(a) The Company does not own any real property. Schedule 5.10(a) sets forth a complete list of all leases of real property by the Company (individually, a "Real Property Lease" and collectively, the "Real Property Leases" or "Company Properties") as lessee or lessor. The Company Properties constitute all interests in real property currently used, occupied or currently held for use in connection with the business of the Company and which are necessary for the continued operation of the business of the Company as the business is currently conducted. The Company has provided Purchaser with true, correct and complete copies of the Real Property Leases, together with all amendments, modifications or supplements, if any, thereto. The Company has a valid, binding and enforceable leasehold interest under each of the Real Property Leases under which it is a lessee, free and clear of all Liens other than Permitted Exceptions. Each of the Real Property Leases is in full force and effect. The Company has not received any written notice of any default or event that with notice or lapse of time, or both, would constitute a default by the Company under any of the Real Property Leases. To the Actual Knowledge of the Company, Holdings and Simmons the landlord is not in material default under any of the Real Property Leases. The Company has not assigned any such lease or sublet all or any part of the Company Properties. Except as described on Schedule 5.10(a), there are no material physical or mechanical defects in any of the Company Properties and each such facility is in the condition and repair required under the Lease.

(b) To the Actual Knowledge of the Company, the Real Property Leases and the Company Properties (and improvements thereon) are presently in compliance with all Laws relating to the Real Property, including the Americans with Disabilities Act, except where the failure to be in compliance would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate. The Company has not received any notice from any party asserting that any of the Real Property Leases or the Company Properties are in violation of any Laws. The Company has not received notice of any pending or threatened condemnation, annexation, special assessments, zoning or subdivision changes, or other adverse claims affecting the Company Properties.

5.11 Tangible Personal Property; Condition of Assets. Schedule 5.11 sets forth a list of all leases of personal property by the Company ("Personal Property Leases") involving annual payments in excess of \$75,000. The Company has not received any written notice of any default or any event that with notice or lapse of time, or both, would constitute a default, by the Company under any of the Personal Property Leases. The furniture, fixtures, machinery, shelving, racks, equipment, tools, dies, molds, jigs, fixtures,

office equipment, business machines, telephones and telephone systems, parts, accessories and other tangible personal property (other than inventory) owned or leased by the Company and used in its operations (collectively, the "Equipment") constitute all tangible personal property necessary in order for the Company to conduct its business as it has been conducted in the past. All Equipment operates substantially in accordance with its specifications, adequately performs the functions it is supposed to perform, is free of any material structural, mechanical, installation or engineering defects and in good operating condition and repair (ordinary wear and tear excepted). The Company possesses good, valid and marketable title to, or valid leaseholder interest in, or valid license to use all the property under the Personal Property Leases and the Equipment used or necessary for the conduct of the business, free and clear of all Liens other than Permitted Exceptions.

#### 5.12 Intellectual Property.

(a) Schedule 5.12(a) sets forth an accurate and complete list of all issued Patents, pending Patent applications, registered Marks, pending applications for registration of Marks, registered Copyrights and Internet domain names owned by the Company.

(b) Except as set forth on Schedule 5.12(b), the Company owns, or possesses adequate licenses or other valid rights to use (in each case, free and clear of any Liens), all Intellectual Property and Technology used by the Company in the Ordinary Course of Business. Without limiting the generality of the foregoing, except as set forth on Schedule 5.12(b), the Company owns all rights, title and interests in and to all of the Marks throughout the respective jurisdictions set forth on Schedule 5.12(a) (free and clear of all Liens), and no Person has or has claimed or alleged any right or interest therein or thereto.

(c) The conduct of the business and operations of the Company and the use of the Intellectual Property and Technology owned by the Company does not infringe or constitute a misappropriation of the Intellectual Property of any Person.

(d) As of the date of this Agreement, there is no pending Legal Proceeding (and the Company has not received written notice of any claim) challenging any right of the Company in or the validity of any Intellectual Property or Technology owned by or exclusively licensed to the Company, which, to the Knowledge of the Company, if adversely determined, would result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate.

(e) Except as set forth on Schedule 5.12(e), As of the date of this Agreement, there are no Orders to which the Company is a party that restrict the Company's right to use any Intellectual Property or Technology used by the Company in the Ordinary Course of Business.

(f) Except as set forth on Schedule 5.12(f), to the Knowledge of the Company, no Person is infringing or misappropriating any Intellectual Property owned by or exclusively licensed to the Company.

(g) To the Knowledge of the Company, no Intellectual Property owned by or exclusively licensed to the Company is invalid or unenforceable.

(h) The Intellectual Property and Technology are sufficient to continue to operate the business of the Company immediately after the Closing as currently conducted. All patents, trademarks, trade names, service marks and copyrights, and all registrations thereof, included in the Intellectual Property owned by the Company, and all Intellectual Property licensed to the Company, are valid and in full force and effect.

#### 5.13 Material Contracts.

(a) Schedule 5.13(a) sets forth all of the following Contracts to which the Company is a party or by which it is bound (collectively, the "Material Contracts"):

(i) Contracts for the employment of any individual on a full-time, part-time or consulting or other basis providing annual compensation in excess of \$75,000;

(ii) Contracts providing for severance, retention, change in control or other similar payments;

(iii) Contracts in which the Company has agreed or is bound not to compete in any manner or geographic area or in any business;

(iv) Contracts limiting the Company's freedom to operate, own, pledge, sell, transfer or otherwise dispose of or encumber any of its assets;

(v) all Contracts regarding capital stock of the Company, including any shareholder agreement, voting or voting trust agreement or proxy;

(vi) Contracts between the Company, on one hand, and Simmons, Holdings or any of their Affiliates or any current officer or director of the Company, on the other hand;

(vii) Contracts with any labor union or association representing any employee of the Company;

(viii) Contracts for the sale of any of the assets of the Company other than in the Ordinary Course of Business;

(ix) Contracts relating to any acquisition to be made by the Company of any operating business or the capital stock of any other Person;

(x) Contracts relating to the incurrence of indebtedness for borrowed money, or the making of any loans, in each case involving amounts in excess of \$75,000;

(xi) Contracts for indemnification, reimbursement, guaranty, suretyship or other obligation to assume or incur any obligation of a third party involving amounts in excess of \$75,000 individually or \$150,000 in the aggregate;

(xii) Contracts for joint ventures, strategic alliances, partnerships, or sharing of profits or proprietary information;

(xiii) Contracts, including distribution, supply and advertising Contracts, which involve the expenditure of more than \$75,000 in the aggregate or require performance by any party more than one year from the date hereof that, in either case, are not terminable by the Company without penalty on notice of 90 days' or less;

(xiv) Real Property Leases set forth on Schedule 5.10;

(xv) Personal Property Leases set forth on Schedule 5.11; and

(xvi) Contracts under which the Company has licensed any material Intellectual Property or material Technology from any third Person or under which the Company licenses any material Intellectual Property or material Technology to any third Person.

(b) All Material Contracts are in full force and binding upon the parties thereto. Except as set forth on Schedule 5.13(b), the Company has not received any notice of any default or event that with notice or lapse of time, or both, would constitute a default by the Company under any Material Contract. The Company has provided Purchaser with true, correct and complete copies of all of the Material Contracts, together with all amendments, modifications or supplements thereto.

#### 5.14 Employee Benefits Plans.

(a) Schedule 5.14(a) lists each employment, bonus, deferred compensation, incentive compensation, stock purchase, stock option, stock appreciation right or other stock-based incentive, severance, change-in-control or termination pay, hospitalization or other medical, disability, life or other insurance, supplemental unemployment benefits, profit-sharing, pension or retirement plan, program, agreement or arrangement and each other material employee benefit plan, program, agreement or arrangement, sponsored, maintained or contributed to or required to be contributed to by the Company for the benefit of any current or former employee, independent contractor or director of the Company (the "Company Plans"). Except for amendments that are required for the Company Plans to meet the requirements of applicable law, tax-qualified status under Section 401(a) of the Code, if applicable, or Section 409A of the Code, if applicable, applicable regulatory guidance, the terms of such Company Plans, the Company has no formal plan or commitment, whether legally binding or not, to create any additional Company Plans or modify or change any existing Company Plan that would materially affect any current or former employee, independent contractor or director of the Company.

(b) With respect to each of the Company Plans, true and complete copies of each of the following documents, as applicable, have been made available to the Purchaser:

(i) a copy of the Company Plan documents (including all amendments thereto) for each written Company Plan or a written description of any Company Plan that is not otherwise in writing;

(ii) a copy of the annual report or Internal Revenue Service Form 5500 Series, if required under ERISA or the Code, with respect to each Company Plan for the last three (3) Plan years ending prior to the date of this Agreement for which such a report was filed;

(iii) a copy of the actuarial report, if required under ERISA, with respect to each Company Plan subject to ERISA (each, an "ERISA Plan") for the last three (3) Plan years ending prior to the date of this Agreement for which a report was required;

(iv) a copy of the most recent Summary Plan Description ("SPD"), together with all Summaries of Material Modification issued with respect to such SPD, if required under ERISA, with respect to each ERISA Plan, and all other material employee communications relating to each ERISA Plan;

(v) if the Company Plan is funded through a trust or any other funding vehicle, a copy of the trust or other funding agreement (including all amendments thereto) and the latest financial statements thereof, if any; and

(vi) the most recent determination letter received from the Internal Revenue Service ("IRS") with respect to each Company Plan that is intended to be qualified under Section 401(a) of the Code.

(c) None of the Company Plans is (or during the prior 6 years has been) subject to Title IV of ERISA.

(d) The Company has not engaged in a transaction or has taken or failed to take any action in connection with a Company Plan that could subject the Company to any material liability for either a civil penalty assessed pursuant to Section 409, 502(i) or 502(l) of ERISA, or a tax imposed pursuant to Section 4975(a) or (b), 4976 or 4980B of the Code.

(e) All contributions and premiums that the Company and each ERISA Affiliate is required to pay under the terms of each of the ERISA Plans and Section 412 of the Code, have, to the extent due, been paid in full or properly recorded on the financial statements or records of the Company consistent with historical practice or as otherwise required by GAAP, and none of the ERISA Plans or any trust established thereunder has incurred any "accumulated funding deficiency" (as defined in Section 302 of ERISA and Section 412 of the Code), whether or not waived, as of the last day of the most recent fiscal year of each of the ERISA Plans ended prior to the date of this Agreement. No lien has been imposed under Section 412(n) of the Code or Section 302(f) of ERISA on the assets of the Company or any ERISA Affiliate, and no event or circumstance has occurred that is reasonably likely to result in the imposition of any such lien on any such assets on account of any ERISA Plan.

(f) Each of the Company Plans has been operated and administered in all material respects in accordance with its terms and applicable laws, including ERISA and the Code.

(g) Each of the ERISA Plans that is intended to be "qualified" within the meaning of Section 401(a) of the Code is so qualified, and with respect to such ERISA Plans, the Company has received a currently effective determination letter from the IRS stating that the ERISA Plan is so qualified, and no event has occurred that would affect such qualified status.

(h) Any fund established under an ERISA Plan that is intended to satisfy the requirements of Section 501(c)(9) of the Code has so satisfied such requirements.

(i) No Company Plan provides benefits coverage, including without limitation death or medical benefits coverage (whether or not insured), with respect to current or former employees of the Company after retirement or other termination of service (other than coverage (i) mandated by applicable laws or (ii) the full direct cost of which is borne by the current or former employee (or beneficiary thereof)).

(j) Except as set forth on Schedule 5.14(a) the consummation of the transactions contemplated by this Agreement will not, either alone or in combination with any other event, (i) entitle any current or former employee, officer or director of the Company to severance pay, unemployment compensation or any other similar termination payment, or (ii) accelerate the time of payment or vesting, or increase the amount of or otherwise enhance any benefit due from the Company to any such employee, officer or director.

(k) There are no pending or, to the Actual Knowledge of the Company, Holdings or Simmons, threatened or anticipated claims by any current or former employee or beneficiary under any Company Plan (other than routine claims for benefits).

5.15 Labor and Employment.

(a) Except as set forth on Schedule 5.15(a), the Company is not a party to any labor or collective bargaining agreement.

(b) Except as set forth on Schedule 5.15(b), there are no (i) strikes, work stoppages, work slowdowns or lockouts pending or, to the Actual Knowledge of the Company, threatened against or involving the Company, (ii) unfair labor practice charges, or grievances or complaints pending or, to the Knowledge of the Company, threatened by or on behalf of any employee or group of employees of the Company, or (iii) union organizational activities existing with respect to the Company's employees that, to the Actual Knowledge of the Company, could reasonably be expected to result in Losses or Liabilities in excess of \$75,000 individually or \$150,000 in the aggregate. Except as set forth on Schedule 5.15(b), no charge is pending nor, to the Company's Actual Knowledge, threatened, against the Company before any court or agency alleging unlawful discrimination in employment practices and no charge or proceeding with regard to any unfair labor practice is pending before the National Labor Relations Board or any other tribunal. No one has petitioned within the last 3 years, and no one is now petitioning the Company, for union representation of any employees of the Company. The Company has not experienced any labor strike, slow-down, stoppage, labor difficulty or other job action during the last 3 years that, individually or in the aggregate, could reasonably be expected to result in Losses or Liabilities in excess of \$75,000 individually or \$150,000 in the aggregate.

(c) Except as set forth in Schedule 5.15(c), the Company: (i) is in compliance with all Laws respecting employment, employment practices, terms and conditions of employment and wages and hours, in each case, with respect to its employees and independent contractors, except where the failure to be in compliance would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate; (ii) has paid, withheld and reported all amounts required by Law or by agreement to be paid in respect of or withheld and reported from the wages, salaries and other payment to employees; (iii) is not liable for any arrears of wages or any Taxes or any penalty relating thereto; and (iv) is not liable for any payment to any trust or other fund relating to Company Plans or to any Governmental Body with respect to unemployment compensation benefits, social security or similar types of benefits mandated by Law for employees (other than routine payments to be made in the Ordinary Course of Business).

5.16 Litigation. Except as set forth on Schedule 5.16, there are no Legal Proceedings pending or, to the Actual Knowledge of the Company, threatened against the Company (or its officers, directors, employees or agents (while acting as an agent of the Company)) or the Company's assets, operations or personnel before any Governmental Body. Except as set forth on Schedule 5.16, the Company is not subject to any Order, and the Company is not in breach or violation of any Order.

5.17 Compliance with Laws; Permits.

(a) The Company is in compliance with all Laws of any Governmental Body applicable to its business or operations, except where the failure to be in compliance would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate.

(b) The Company has not received any written notice of or been charged with the violation of any Laws, except where such violation would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate.

(c) The Company currently has all Permits which are required for the operation of their respective businesses as presently conducted, other than those the failure of which to possess would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate. The Company is not in default or violation (and no event has occurred which, with notice or the lapse of time or both, would constitute a default or violation) of any term, condition or provision of any Permit to which it is a party, except where such default or violation would not result in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate.

5.18 Environmental Matters. Except as set forth on Schedule 5.18 hereto:

(a) the operations of the Company are in material compliance with all applicable Environmental Laws, which compliance includes obtaining, maintaining and complying in all material respects with any Permits required under all applicable Environmental Laws necessary to operate its business ("Environmental Permits");

(b) the Environmental Permits are valid and in full force and effect, and are transferable;

(c) the Company is not subject to any pending, or to the Actual Knowledge of the Company, threatened claim alleging that the Company may be in violation of any Environmental Law or any Environmental Permit or may have any Liability under any Environmental Law;

(d) there are no pending or, to the Actual Knowledge of the Company, threatened investigations of the business of the Company, or any currently or previously owned or, to the Actual Knowledge of the Company, leased property of the Company under Environmental Laws, which would reasonably be expected to result in the Company incurring any material liability pursuant to any Environmental Law;

(e) No Hazardous Material has been Released by the Company, at, on or under the Real Property as to which Remedial Action is required under any Environmental Law within the past 3 years or, to the Actual Knowledge of the Company, at any time prior thereto;

(f) the Company has not received any notice of any private, administrative or judicial action, or notice of any intended private, administrative or judicial action relating to the presence or alleged presence of Hazardous Material in, under, upon or emanating from any of the real property now or during the 3 years prior to the Closing Date owned or leased by the Company; and

(g) there are no environmental audits or investigation reports conducted within the last 5 years in the possession of the Company relating to the Real Property or any Company operations thereon which have not been previously provided to the Purchaser.

5.19 Suppliers. Since the Balance Sheet Date, none of the 10 largest suppliers of bedding products to the Company, as measured by the dollar amount of purchases thereby during fiscal year 2005, has terminated its relationship with the Company or materially reduced or changed the pricing or other terms of its business with the Company and no such supplier has notified the Company in writing that it intends to terminate or materially reduce or change the pricing or other terms of its business with the Company.

5.20 Financial Advisors. No Person has acted, directly or indirectly, as a broker, finder or financial advisor for Holdings or the Company in connection with the transactions contemplated by this Agreement and no such Person is entitled to any fee or commission or like payment from Purchaser in respect thereof.

5.21 Insurance. Schedule 5.21 is a complete list of all insurance policies currently in effect, or with respect to “occurrence” policies, that were in effect during the 3 years prior to the date hereof, that relate to operation of the business, or cover the Real Property. Schedule 5.21 summarizes the following information for each such policy: the name of the insurer, the type of risks insured, the deductible and limits of coverage and the annual premium. True and complete copies of such policies have been made available to the Purchaser. During the last three (3) years, no material insurance coverage of the Company has lapsed. The Company is not in default or breach with respect to any provision contained in any such insurance policies, nor has the Company failed to give any notice or to present any claim thereunder in due and timely fashion.

5.22 Related Party Transactions. Schedule 5.22 is an accurate list of the accounts and notes receivable of the Company from and advances to employees, former employees, officers, directors, shareholders and any Affiliate of the foregoing which have not been fully repaid (other than advances provided to employees in connection with the performance of their duties in the Ordinary Course of Business which do not exceed \$5,000 in any one instance). Neither Holdings nor any of its Affiliates has entered into any transaction with or is a party to any agreement, lease or other instrument or arrangement, or as of the Closing Date is indebted to or is owed money by the Company that is not disclosed in the Financial Statements. Except as disclosed in the Financial Statements, neither Simmons nor any of its Subsidiaries owns any direct or indirect interest of any kind in, or controls or is a director, officer, employee, shareholder or partner of, or consultant or lender to or borrower from or has the right to participate in the profits of, any Person which is a competitor, supplier, customer, landlord, tenant, creditor or debtor of the Company.

5.23 No Other Representations or Warranties; Schedules. Except for the representations and warranties contained in this Article V and Article VI (each as modified by the Schedules thereto), neither Simmons, Holdings, the Company nor any other Person makes any other express or implied representation or warranty with respect to the Company or the transactions contemplated by this Agreement, and the Company disclaims any other representations or warranties, whether made by the Company, Holdings, Simmons or any of their respective Affiliates, officers, directors, employees, agents or representatives. Except for the representations and warranties contained in Article V and Article VI hereof (each as modified by the Schedules thereto as supplemented or amended), the Company, Holdings and Simmons hereby disclaim all liability and responsibility for any representation, warranty, projection, forecast, statement, or information made, communicated, or furnished (orally or in writing) to Purchaser or its Affiliates or representatives (including any opinion, information, projection, or advice that may have been or may be provided to Purchaser by any director, officer, employee, agent, consultant, or representative of the Company or any of their respective Affiliates). The Company, Holdings and Simmons make no representations or warranties to Purchaser regarding the probable success or profitability of the Company.

## ARTICLE VI

### REPRESENTATIONS AND WARRANTIES OF HOLDINGS AND SIMMONS

Holdings and Simmons hereby represent and warrant to Purchaser that:

6.1 Organization and Good Standing. Each of Holdings and Simmons is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and each has all requisite corporate power and authority to own, lease and operate its respective properties and to carry on its respective business.

6.2 Authorization of Agreement. Each of Holdings and Simmons has all requisite corporate power, authority and legal capacity to execute and deliver this Agreement and each other agreement, document, or instrument or certificate contemplated by this Agreement or to be executed by Holdings and Simmons in connection with the consummation of the transactions contemplated by this Agreement (together with this Agreement, the “Simmons Documents”), and to consummate the transactions contemplated hereby and thereby. The execution and delivery of this Agreement and each of the Simmons Documents and the consummation of the transactions contemplated hereby and thereby have been duly authorized by all required corporate action on the part of Holdings and Simmons. This Agreement has been, and each of the Simmons Documents will be at or prior to the Closing, duly and validly executed and delivered by Holdings and Simmons, and (assuming the due authorization, execution and delivery by the other parties hereto and thereto) this Agreement constitutes, and each Simmons Document, when so executed and delivered will constitute, the legal, valid and binding obligation of Holdings and Simmons, enforceable against Holdings and Simmons in accordance with its terms, subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors’ rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity).

6.3 Conflicts; Consents of Third Parties. Except as set forth on Schedule 6.3:

(a) None of the execution and delivery by Holdings and Simmons of this Agreement or the Simmons Documents, the consummation of the transactions contemplated hereby or thereby, or compliance by Holdings and Simmons with any of the provisions hereof or thereof will conflict with, or result in any violation of or default (with or without notice or lapse of time, or both) under, or give rise to a right of termination or cancellation under, any provision of (i) the respective certificates of incorporation and by-laws (or other organizational and governing documents) of Holdings and Simmons; (ii) any Contract, or Permit to which Holdings or Simmons is a party or by which any of the properties or assets of Holdings or Simmons are bound; (iii) any Order of any Governmental Body applicable to Holdings or Simmons or by which any of the respective properties or assets of Holdings or Simmons are bound; or (iv) any applicable Law.

(b) No consent, waiver, approval, Order, Permit or authorization of, or declaration or filing with, or notification to, any Person or Governmental Body is required on the part of Holdings or Simmons in connection with the execution and delivery of this Agreement or the Simmons Documents, or the compliance by Holdings and Simmons with any of the provisions hereof or thereof, the consummation of the transactions contemplated hereby, except for (A) compliance with the applicable requirements of the HSR Act and (B) for such other consents, waivers, approvals, Orders, permits or authorizations the failure of which to obtain would not have a material adverse effect on Holdings’ or Simmons’ ability to consummate the transactions contemplated hereby.

6.4 Ownership and Transfer of Units. Holdings is the record and beneficial owner of the Shares, and as of the Closing Date will be the owner of the Units, free and clear of any and all Liens. Holdings has the corporate power and authority to sell, transfer, assign and deliver such Units as provided in this Agreement, and such delivery will convey to Purchaser good and marketable title to such Units, free and clear of any and all Liens.

6.5 Litigation. There are no Legal Proceedings pending or, to the Actual Knowledge of Holdings and Simmons threatened that are reasonably likely to prohibit or restrain the ability of Holdings or Simmons to enter into this Agreement or consummate the transactions contemplated hereby.

6.6 Financial Advisors. No Person has acted, directly or indirectly, as a broker, finder or financial advisor for Holdings or Simmons in connection with the transactions contemplated by this Agreement and no Person is entitled to any fee or commission or like payment in respect thereof.

## ARTICLE VII

## REPRESENTATIONS AND WARRANTIES OF PURCHASER

Purchaser hereby represents and warrants to Holdings and Simmons that:

7.1 Organization and Good Standing. Purchaser is a limited liability company duly formed, validly existing and in good standing under the laws of the State of California and has all requisite limited liability power and authority to own, lease and operate properties and carry on its business.

7.2 Authorization of Agreement. Purchaser has full limited liability company power and authority to execute and deliver this Agreement and each other agreement, document, instrument or certificate contemplated by this Agreement or to be executed by Purchaser in connection with the consummation of the transactions contemplated hereby and thereby (the "Purchaser Documents"), and to consummate the transactions contemplated hereby and thereby. The execution, delivery and performance by Purchaser of this Agreement and each Purchaser Document have been duly authorized by all necessary limited liability company, action on behalf of Purchaser. This Agreement has been, and each Purchaser Document will be at or prior to the Closing, duly executed and delivered by Purchaser and (assuming the due authorization, execution and delivery by the other parties hereto and thereto) this Agreement constitutes, and each Purchaser Document when so executed and delivered will constitute, the legal, valid and binding obligation of Purchaser, enforceable against Purchaser in accordance with its terms, subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors' rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity).

7.3 Conflicts; Consents of Third Parties.

(a) Except as set forth on Schedule 7.3(a) hereto, none of the execution and delivery by Purchaser of this Agreement or the Purchaser Documents, the consummation of the transactions contemplated hereby or thereby, or the compliance by Purchaser with any of the provisions hereof or thereof will conflict with, or result in any violation of or default (with or without notice or lapse of time, or both) under, or give rise to a right of termination or cancellation under, any provision of (i) the organizational or governing documents of Purchaser; (ii) any Contract or Permit to which Purchaser is a party or by which Purchaser or its properties or assets are bound; (iii) any Order of any Governmental Body applicable to Purchaser or by which any of the properties or assets of Purchaser are bound; or (iv) any applicable Law.

(b) No consent, waiver, approval, Order, Permit or authorization of, or declaration or filing with, or notification to, any Person or Governmental Body is required on the part of Purchaser in connection with the execution and delivery of this Agreement or the Purchaser Documents, the compliance by Purchaser with any of the provisions hereof or thereof, the consummation of the transactions contemplated hereby or the taking by Purchaser of any other action contemplated hereby, except for compliance with the applicable requirements of the HSR Act.

7.4 Litigation. There are no Legal Proceedings pending or, to the actual knowledge of Purchaser (without any docket or other electronic search having been conducted), threatened that are reasonably likely to prohibit or restrain the ability of Purchaser to enter into this Agreement or consummate the transactions contemplated hereby.

7.5 Investment Intention. Purchaser is acquiring the Units for its own account, for investment purposes only and not with a view to the distribution (as such term is used in Section 2(11) of the Securities Act of 1933, as amended (the "Securities Act") thereof. Purchaser understands that the Units have not been registered under the Securities Act and cannot be sold unless subsequently registered under the Securities Act or an exemption from such registration is available.

7.6 Financial Advisors. No Person has acted, directly or indirectly, as a broker, finder or financial advisor for Purchaser in connection with the transactions contemplated by this Agreement and no Person is entitled to any fee or commission or like payment in respect thereof.

7.7 Financing. Schedule 7.7 sets forth complete and correct copies of a commitment letter from Wells Fargo (the "Financing Commitment") for the debt financing to be used in connection with the transactions contemplated hereby (the "Financing"). The amount of the Financing, if obtained, together with financing to be provided by Purchaser and its Affiliates, will provide sufficient funds for Purchaser to consummate the transactions contemplated by this Agreement.

7.8 Condition of the Business. Notwithstanding anything contained in this Agreement to the contrary, Purchaser acknowledges and agrees that neither the Company, Holdings nor Simmons is making any representations or warranties whatsoever, express or implied, beyond those expressly given by the Company, Holdings and Simmons, as the case may be, in Article V and Article VI, respectively (as modified by the Schedules hereto as supplemented or amended). Any claims Purchaser may have for breach of representation or warranty shall be based solely on the representations and warranties of the Company, Holdings or Simmons set forth in Article V or Article VI, respectively (as modified by the Schedules hereto as supplemented or amended). Purchaser further represents that none of the Company, Holdings, Simmons or any of their respective Affiliates nor any other Person has made any representation or warranty, express or implied, as to the accuracy or completeness of any information regarding the Company, Holdings, Simmons or the transactions contemplated by this Agreement not expressly set forth in this Agreement, and none of the Company, Holdings, Simmons any of their respective Affiliates or any other Person will have or be subject to any liability to Purchaser or any other Person resulting from the distribution to Purchaser, its Affiliates or their representatives or Purchaser's or its Affiliates use of, any such information, or other publications or data room information provided to Purchaser, its Affiliates or their representatives, or any other document or information in any form provided to Purchaser, its Affiliates or their representatives in connection with the sale of the Company and the transactions contemplated hereby. Purchaser acknowledges that it has conducted to its satisfaction, its own independent investigation of the condition, operations and business of the Company.

## ARTICLE VIII

### COVENANTS

8.1 Access to Information. Prior to the Closing, Purchaser shall be entitled, through its officers, employees and representatives (including its legal advisors and accountants), to make such investigation of the properties, businesses and operations of the Company, including an audit of the Company's inventory, and such examination of the books and records of the Company as it reasonably requests and to make extracts and copies of such books and records. Any such investigation and examination shall be conducted during regular business hours upon reasonable advance notice and under reasonable circumstances and shall be subject to restrictions under applicable Law. The Company shall cause the officers, employees, consultants, agents, accountants, attorneys and other representatives of the Company to cooperate with Purchaser and its representatives in connection with such investigation and examination, and Purchaser and its representatives shall cooperate with the Company and its representatives and shall use their reasonable efforts to minimize any disruption to the business.

## 8.2 Conduct of the Business Pending the Closing.

(a) Prior to the Closing, except (I) as set forth on Schedule 8.2, (II) as required by applicable Law, (III) as otherwise contemplated by this Agreement or (IV) with the prior written consent of Purchaser, the Company shall:

- (i) conduct the business of the Company only in the Ordinary Course of Business and not introduce any new method, or discontinue any existing method, of operation or accounting;
- (ii) use its commercially reasonable efforts to (A) preserve the present business operations, organization and goodwill of the Company, and (B) preserve the present relationships with suppliers of the Company;
- (iii) maintain its properties and facilities, including those held under the Real Property Leases, in as good working order and condition as at present, ordinary wear and tear excepted;
- (iv) file on a timely basis (or properly file for extensions) all notices, reports or other filings required to be filed with or reported to any Governmental Body with respect to the continuing operations of the Company; and
- (v) perform in all material respects in the Ordinary Course of Business, its obligations under all Material Contracts and comply with the terms and conditions of all licenses and Permits and all applicable Laws.

(b) Except (I) as set forth on Schedule 8.2, (II) as required by applicable Law, (III) as otherwise contemplated by this Agreement (including the Conversion) or (IV) with the prior written consent of Purchaser (which consent shall not be unreasonably withheld, delayed or conditioned), the Company shall not:

- (i) declare, set aside, make or pay any dividend or other distribution (other than the distribution of Excess Cash to Holdings as contemplated herein or the payment of inter-company Liabilities) in respect of the capital stock of the Company or repurchase, redeem or otherwise acquire any outstanding securities of, or other ownership interests in, the Company;
  - (ii) transfer, issue, sell or dispose of any shares of capital stock or other securities of the Company or grant options, warrants, calls or other rights to purchase or otherwise acquire shares of the capital stock or other securities of the Company;
  - (iii) effect any recapitalization, reclassification or like change in the capitalization of the Company;
  - (iv) amend the certificate of incorporation or by-laws of the Company;
  - (v) other than as required by Law or any written Contract or Company Plan (as disclosed in Schedule 5.14(a)) (A) increase the annual level of compensation of any director, officer, employee, consultant or agent of the Company other than in the Ordinary Course of Business, (B) grant any unusual or extraordinary bonus, benefit or other direct or indirect compensation to any director, officer, employee, consultant or agent, (C) materially increase the coverage or benefits available under any (or create any new) Company Plan or (D) enter into any employment, deferred compensation, severance, consulting, non-competition or similar agreement (or amend any such agreement) to which the Company is a party or involving a director or executive officer of the Company;
  - (vi) subject to any Lien, any of the properties or assets (whether tangible or intangible) of the Company, except for Permitted Exceptions;
  - (vii) acquire any properties, rights or assets or sell, assign, license, transfer, convey, lease or otherwise dispose of any of the properties, rights or assets of the Company (except as contemplated by (i) above or pursuant to an existing Contract for fair consideration in the Ordinary Course of Business or for the purpose of disposing of obsolete or worthless assets) to any Person, including Simmons, Holdings or any Affiliate thereof;
  - (viii) modify, amend, terminate any of the existing Real Property Leases or enter into any construction contracts with respect to improvements or alterations with respect to any of the Real Property Leases for an amount in excess of \$75,000;
  - (ix) cancel or compromise any material debt or claim or waive or release any right of the Company;
  - (x) enter into, modify or terminate any labor or collective bargaining agreement of the Company;
  - (xi) permit the Company to enter into or agree to enter into any merger or consolidation with any Person;
  - (xii) make or rescind any material election relating to Taxes, or settle or compromise any material claim, action, suit, litigation, proceeding, arbitration, investigation, audit or controversy relating to Taxes;
  - (xiii) issue, create, incur, assume, guarantee, endorse or otherwise become liable or responsible with respect to (whether directly, contingently or otherwise) any indebtedness for borrowed money (in excess of such amount set forth on the Balance Sheet);
  - (xiv) enter into any transaction or Contract relating primarily to the Company involving obligations or payments in excess of \$75,000 in any year;
- or
- (xv) agree to do anything prohibited by this Section 8.2.

8.3 Consents. The Purchaser and the Company shall use their commercially reasonable efforts, and Simmons and Holdings shall cooperate with Purchaser and the Company, to obtain at the earliest practicable date all consents and approvals required to consummate the transactions contemplated by this Agreement, including, without limitation, the consents and approvals referred to in Sections 5.3(b) and 7.3(b) hereof (and Simmons shall use its commercially reasonable efforts to obtain at the earliest practicable date all consents under Section 6.3(b)); provided, however, that no party shall be obligated to pay any consideration to any third party from whom consent or approval is requested except for any payment which is required to be made under the terms of any Contract. In addition, the Company will request from, and use good faith efforts to obtain, an estoppel certificate ("Estoppel Certificates") from the landlords under all Real Estate Leases to which the Company is a party in the form attached hereto as Exhibit B.

8.4 Regulatory Approvals. Each of Purchaser, the Company and Holdings (if necessary) shall (a) make or cause to be made all filings required of each of them or any of their respective Affiliates under the HSR Act or the Sherman Act, as amended, the Clayton Act, as amended, the Federal Trade Commission Act, as amended, and any other United States federal or state or foreign statutes, rules, regulations, orders, decrees, administrative or judicial doctrines or other laws that are designed to prohibit, restrict or regulate actions having the purpose or effect of monopolization or restraint of trade (collectively, the “Antitrust Laws”) with respect to the transactions contemplated hereby as promptly as practicable and, in any event, within one (1) Business Day after the date of this Agreement in the case of all filings required under the HSR Act (and such filing shall request early termination of the waiting period under the HSR Act), (b) comply at the earliest practicable date with any request under the HSR Act or other Antitrust Laws for additional information, documents, or other materials received by each of them or any of their respective subsidiaries or Affiliates from the FTC, the Antitrust Division or any other Governmental Body in respect of such filings or such transactions, and (c) cooperate with each other in connection with any such filing (including, to the extent permitted by applicable law, providing copies of all such documents to the non-filing parties prior to filing and considering all reasonable additions, deletions or changes suggested in connection therewith) and in connection with resolving any investigation or other inquiry of any of the FTC, the Antitrust Division or other Governmental Body under any Antitrust Laws with respect to any such filing or any such transaction. Each such party shall use its reasonable best efforts to furnish to each other all information required for any application or other filing to be made pursuant to any applicable law in connection with the transactions contemplated by this Agreement. Each such party shall promptly inform the other parties hereto of any oral communication with, and provide copies of written communications with, any Governmental Body regarding any such filings or any such transaction. No party hereto shall independently participate in any formal meeting with any Governmental Body in respect of any such filings, investigation, or other inquiry without giving the other parties hereto prior notice of the meeting and, to the extent permitted by such Governmental Body, the opportunity to attend and/or participate. Subject to applicable Law, the parties hereto will consult and cooperate with one another in connection with any analyses, appearances, presentations, memoranda, briefs, arguments, opinions and proposals made or submitted by or on behalf of any party hereto relating to proceedings under the HSR Act or other Antitrust Laws. Any party may, as it deems advisable and necessary, reasonably designate any competitively sensitive material provided to the other parties under this Section 8.4 as “outside counsel only.” Such materials and the information contained therein shall be given only to the outside legal counsel of the recipient and will not be disclosed by such outside counsel to employees, officers, or directors of the recipient, unless express written permission is obtained in advance from the source of the materials.

8.5 Further Assurances. Subject to, and not in limitation of, Section 8.4, each of Purchaser, Simmons and the Company shall use its commercially reasonable efforts to (i) take all actions necessary or appropriate to consummate the transactions contemplated by this Agreement and (ii) cause the fulfillment at the earliest practicable date of all of the conditions to their respective obligations to consummate the transactions contemplated by this Agreement.

8.6 Confidentiality. Purchaser acknowledges that the information provided to it in connection with this Agreement and the transactions contemplated hereby is subject to the terms of the confidentiality agreement between Sleep Train, Inc. and the Company dated June 7, 2006 (the “Confidentiality Agreement”), the terms of which are incorporated herein by reference.

8.7 Preservation of Records. Holdings, Simmons and Purchaser agree that each of them shall preserve and keep the records held by them or their Affiliates relating to the business of the Company for a period of 7 years from the Closing Date and shall make such records and personnel available to the other as may be reasonably required by such party in connection with, among other things, any insurance claims by, Legal Proceedings or Tax audits against or governmental investigations of Simmons, Holdings or Purchaser or any of their Affiliates or in order to enable Holdings, Simmons or Purchaser to comply with their respective obligations under this Agreement and each other agreement, document or instrument contemplated hereby or thereby. In the event Holdings, Simmons or Purchaser wishes the other party to continue to maintain such records after that time, such party shall first give 90 days prior written notice to the other and such party shall have the right at its option and expense, upon prior written notice given to such other party within that 90 day period, to take possession of the records within 180 days after the date of such notice.

#### 8.8 Publicity.

(a) None of Holdings, Simmons, the Company, Purchaser or their Affiliates shall issue any press release or public announcement concerning this Agreement or the transactions contemplated hereby without obtaining the prior written approval of the other party hereto, which approval will not be unreasonably withheld or delayed, unless, in the sole judgment of Holdings, Simmons, the Company or Purchaser, as applicable, disclosure is otherwise required by applicable Law or by the applicable rules of any stock exchange on which Holdings, Simmons, the Company or Purchaser lists securities, provided that, to the extent required by applicable Law, the party intending to make such release shall use its commercially reasonable efforts consistent with such applicable Law to consult with the other party with respect to the timing and content thereof.

(b) Each of Purchaser, the Company, Simmons, and Holdings acknowledge and agree that Simmons shall have the right to file this Agreement (without schedules and exhibits) with the Securities and Exchange Commission, making the Agreement publicly available, and each party hereto further shall have the right to make such other public disclosures to the extent required by Law.

#### 8.9 Employee Benefits.

(a) Purchaser intends to continue in effect the Company Plans on and after the Closing Date through the respective insurance coverage periods thereof (or, if terminated early, replace any such Company Plan with a reasonably comparable plan) on behalf of each employee of the Company who continues in the employment of the Company or its Affiliates (a “Continuing Employee”). Purchaser hereby agrees to cause the Company to make a payment at the end of the Company’s fiscal year to the Company’s 401(k) Profit Sharing Plan in an amount at least equal to the amount accrued by the Company as of the Closing Date and included in the Actual Closing Date Working Capital.

(b) If Company Plans are replaced as set forth above, then for purposes of eligibility and vesting (but not benefit accrual) under the employee benefit plans of Purchaser or its Affiliates providing benefits to Continuing Employees (the “Purchaser Plans”), Purchaser shall credit each Continuing Employee with his or her years of service with the Company and any predecessor entities, to the same extent as such Continuing Employee was entitled immediately prior to the Closing to credit for such service under any similar Company Plan. To the extent not prohibited by the Purchaser Plans, Purchaser shall not deny Continuing Employees coverage on the basis of pre-existing conditions (to the extent provided under an applicable Company Plan) and shall credit such Continuing Employees for any deductibles and out-of-pocket expenses paid in the year of initial participation in the Purchaser Plans.

8.10 Supplementation and Amendment of Schedules. From time to time prior to the Closing, the Company shall have the right to supplement or amend the Schedules with respect to any matter hereafter arising or discovered after the delivery of the Schedules pursuant to this Agreement (the “Supplemental Material”). No Supplemental Material shall have any effect on the satisfaction of the condition to closing set forth in Section 9.1(a). If the Supplemental Material discloses facts that would constitute (in the absence of any amendment to the Schedules for such Supplemental Material) a breach of the Company, Holdings or Simmons’ representations and warranties hereunder and such breach would have a Material Adverse Effect, the Company shall have 15 days to cure any such breach, and if not cured within such 15-day period, the Purchaser may terminate this Agreement by delivering a termination notice to the Company within 10 days after expiration of the 15-day cure period. The termination notice must specify the representation or warranty breached, identify the specific facts in the Supplemental Material that constitute the breach, and describe why the breach would have a Material Adverse Effect. If the Agreement shall not have been terminated during such 10-day period, the Purchaser shall have waived the right to terminate the Agreement based on such Supplemental Material.

8.11 Non-Competition by Holdings, Simmons and their Subsidiaries. In consideration of the benefits of this Agreement to Holdings and Simmons and in order to induce Purchaser to enter into this Agreement, Holdings and Simmons hereby covenant and agree as follows:

(a) from and after the Closing and until the earlier to occur of (1) the fourth anniversary of the Closing Date and (2) the date upon which a Simmons Sale (as defined below) occurs, Holdings, Simmons and their Subsidiaries shall not, directly or indirectly, as a partner, stockholder, proprietor, joint venturer, or investor, and whether for the benefit of Holdings, Simmons, any of their Subsidiaries, or any other Person: engage in, or own, manage, operate or control, any business or entity which engages anywhere in the States of Washington and Oregon (the “Territory”) in the business of the retail sale of mattresses and bedding products; provided, however, that nothing herein shall prohibit Holdings, Simmons or their Subsidiaries from (i) selling mattresses to other dealers, provided that the terms of any such sales shall not breach the Dealer Incentive Agreement; or (ii) owning, in the aggregate, not more than two percent (2%) of any class of securities of a publicly traded entity in any of the foregoing lines of business so long as neither Holdings, Simmons nor any of their Subsidiaries participates in any way in the management, operation or control of such entity; or (iii) operating discount outlet stores solely for the sale of (A) Simmons’ salvage, discontinued, returned or excess products or floor samples, (B) products of licensees of Simmons or its Affiliates, and (iii) inventory from dealers which Simmons agrees to sell on such dealers’ behalf in order to create space at a dealer’s location for Simmons’ products; provided that such outlet stores will be limited to those in operation as of the Closing Date plus one additional outlet store in each of the States of Oregon and Washington (y) of comparable floor space as any pre-existing outlet store and (x) in a comparable location as Simmons’ existing outlet stores; or (iv) entering into a retail business dedicated exclusively to Luxury Products (as defined below) distributed by Windsor Bedding Co., LLC, a Subsidiary of Simmons, or a successor company or Affiliates; or (v) selling products directly to consumers via the internet or permitting dealers to sell products directly to consumers via the internet; or (vi) ownership in a dealer or retail store pursuant to the foreclosure of any pledge of interests in such dealer or retail store to secure any obligations owed to Simmons or any of its Subsidiaries; provided that, Simmons shall use commercially reasonable efforts to divest itself of any such dealer, stores or assets and shall provide Purchaser a right of first refusal to purchase such interests.

As used herein, “Luxury Products” means mattresses and bedding-related products where the mattresses are offered or sold at price points higher than the top-of-the-line products offered by the Company or Simmons’ then current top 10 dealers (by volume) (i.e. it being understood that “Luxury Products” excludes any product or line of products being sold by the Company as of the Closing Date).

As used herein, “Simmons Sale” means solely: (1) a sale of all, or substantially all, of the assets of Simmons and its Subsidiaries, taken as a whole, to an independent third party, or (2) the acquisition by a person or group of related persons (other than the existing stockholders of Simmons) of more than 50% of the voting securities of Simmons, in each case in which the acquirer shall have been, at the time of such acquisition and throughout the 6-month period prior thereto, already engaged in the retail sale of mattresses or bedding products in the States of Oregon and Washington.

(b) Holdings and Simmons acknowledge that, given the nature of the business of Purchaser and the Company, the covenants contained in this Section 8.11 contain reasonable limitations as to time, geographical area and scope of activity to be restrained, and do not impose a greater restraint than is necessary to protect and preserve for the benefit of Purchaser the goodwill of the Company and to protect the legitimate business interests of Purchaser. If, however, this Section 8.11 is determined by any court of competent jurisdiction to be unenforceable by reason of its extending for too long a period of time or over too large a geographic area or by reason of its being too extensive in any other respect or for any other reason it will be interpreted to extend only over the longest period of time for which it may be enforceable and/or over the largest geographical area as to which it may be enforceable and/or to the maximum extent in all other aspects as to which it may be enforceable, all as determined by such court and in such action. Holdings and Simmons agree that Purchaser’s remedies at law for any breach or threat of breach by Holdings or Simmons of the provisions of this Section 8.11 may be inadequate, and that Purchaser shall be entitled to seek an injunction or injunctions, without the necessity for the posting of a bond or other collateral security, to prevent breaches of the provisions of this Section 8.11 and to seek enforcement specifically the terms and provisions hereof.

#### 8.12 Insurance.

(a) Coverage of the Company under all insurance policies maintained by Simmons shall cease for post-Closing incidents, acts, events or occurrences. From and after the Closing, Purchaser will be responsible for obtaining and maintaining all insurance coverages for the Company for post-closing incidents in their own right. All current policies maintained by Simmons under which the Company has coverage, which policies are identified as “Shared Policies” on Schedule 5.21 hereto (the “Shared Policies”) will be retained by Simmons, together with all rights, benefits and privileges thereunder (including the right to receive any and all return premiums with respect thereto). From and after the Closing, the Company will have the right to assert claims for any loss, liability or damage with respect to the Company (i) under Shared Policies with third party insurers that are “occurrence basis” insurance policies (“Occurrence Basis Policies”) arising out of insured incidents occurring from the date coverage thereunder first commenced until the Closing; (ii) under Shared Policies with third party insurers that are insurance policies written on a “claims made” basis (“Claims Made Policies”) arising out of insured incidents occurring from the date coverage thereunder first commenced until the Closing; and (iii) Simmons will keep the Company, its officers, directors and employees as named insureds under Claims Made Policies (Director’s and Officers, Employment Practices and Fiduciary Liability) for claims arising out of insured incidents occurring from the date of coverage thereunder first commenced until the Closing and for a discovery period of five (5) years post-Closing, or comparable policies with the same or substantially similar terms and conditions. Notwithstanding the foregoing, it is understood and agreed that the retention by the Company of the benefit of Occurrence Basis Policies or Claims Made Policies shall, to the extent such coverage also exists with respect to Simmons or any of its current or former Affiliates (other than the Company), be without prejudice to the rights of Simmons or such other current or former Affiliates (other than the Company) to continue to retain the benefit of such policies at and after the Closing Date as such policies were in effect on the date prior to the Closing Date. Simmons’ and Holdings’ obligation to use reasonable best efforts to assist the Company and Purchaser in asserting claims under applicable Shared Policies will include using commercially reasonable efforts in assisting the Company and Purchaser to establish their right to coverage under such Shared Policies.

(b) Purchaser, the Company and Simmons agree that any claims made under the insurance policies referred to herein in respect of the Company and as to which coverage remains available after Closing shall be administered and collected by Simmons (or by a claims handler appointed by Simmons) on behalf of Purchaser and the Company. Purchaser and the Company shall cooperate fully with Simmons to enable Simmons to comply with the requirements of the relevant insurer, and Purchaser and the Company shall provide such information and assistance as Simmons may reasonably request in connection with any such claim. Any monies received by Simmons as a result of such claims shall be paid over to the Company or Purchaser, net (to the extent such monies are not being paid over to Purchaser pursuant to Simmons’ indemnity obligations under Article X) of all reasonable costs and expenses of recovery (including, without limitation, all reasonable handling and collection charges by any claims handler appointed by Simmons).

#### 8.13 Tax Matters.

(a) Simmons shall prepare or cause to be prepared and either the Company or Simmons, as appropriate, shall file all Tax Returns with respect to the Company for all taxable periods ending on or prior to the Closing Date (“Pre-Closing Periods”). Except as required by Law, without the prior written consent of Simmons (which consent shall not be unreasonably withheld), neither the Company, Purchaser nor any Affiliate of the Company or Purchaser shall file any amended Tax Return with respect to any Pre-Closing Period. To the extent permitted by applicable Law, the Company shall not carry back any Tax attribute to any such period. For the avoidance of doubt, (i) all management bonuses, severance payments, interest payments and deductible financing costs and expenses accrued or paid by the Company on or prior to the Closing Date shall be treated as incurred in a Pre-Closing Period or the pre-Closing portion of a Straddle Period, and (ii) all transactions outside of the ordinary course of business occurring after the Closing shall not be treated as occurring in a Pre-Closing Period or the pre-Closing portion of a Straddle Period. Purchaser shall prepare or cause to be prepared and file all Tax Returns with

respect to the Company for all taxable periods that begin before and end after the Closing Date (“Straddle Periods”); provided that all such Tax Returns shall be prepared in manner that is consistent with the prior practice of the Company. Purchaser shall deliver to Simmons copies of each such Tax Return relating to Straddle Periods, along with a statement (a “Tax Statement”) showing the pre-Closing portion of any Tax Liability required to be paid with such Tax Return (computed in accordance with Section 8.13(b)), at least 20 days prior to the due date for filing such Tax Return, and shall permit Simmons to review and comment on such Tax Return and Tax Statement prior to filing. Purchaser shall not file any such Tax Return relating to Straddle Periods without the prior written consent of Simmons (which shall not be unreasonably withheld or delayed). If the parties have not resolved any dispute relating to any such Tax Return prior to the due date for filing such Tax Return, then Purchaser shall file such Tax Return as prepared, but such filing shall not prejudice the rights of any party to pursue such dispute. If the parties cannot resolve the dispute then any disputed matter shall be submitted to the Arbitrator for resolution, which resolution shall be binding on the parties.

(b) Simmons shall pay or cause to be paid all Taxes of the Company that are allocable to Pre-Closing Periods and the pre-Closing portion of Straddle Periods. With respect to a Straddle Period, the parties hereto will, to the extent permitted by applicable Law, elect with the relevant Taxing Authorities to treat for all purposes the Closing Date as the last day of a taxable period of the Company, and such period shall be treated as a Pre-Closing Period for purposes of this Agreement. In any case where applicable Law does not permit the Company to treat the Closing Date as of the last day of a taxable period, then for purposes of this Agreement, the portion of such Taxes that is attributable to the pre-Closing portion of a Straddle Period shall be (i) in the case of Taxes that are not based on income or gross receipts, the total amount of such Taxes for the period in question multiplied by a fraction, the numerator of which is the number of days in the period up to the Closing Date, and the denominator of which is the total number of days in the entire period in question, and (ii) in the case of Taxes that are based on income or gross receipts, the Taxes that would be due with respect to the period up to the Closing Date, if such period were a taxable period.

(c) Purchaser shall indemnify Simmons and Holdings for any Extra Taxes incurred by Simmons or Holdings. The term “Extra Taxes” shall mean the excess (on a fully grossed-up after-Tax basis), if any, of (A) any Taxes actually paid by Simmons or Holdings on the sale of all of the units of the Company pursuant to a transaction whereby the Company prior to the Closing effects a Conversion over (B) the actual amount of Taxes that would have been paid by Simmons or Holdings on the sale of all of the capital stock of the Company pursuant to a transaction in which the Company, in lieu of a Conversion, remained a corporation and an election under Section 338(h)(10) of the Code was made by the parties. If between the date of this Agreement and the Conversion (which shall occur one Business Day prior to the Closing Date) any of the parties (or any of their respective advisers) determines that Extra Taxes actually may be incurred by virtue of the Conversion, such party shall notify the other party promptly and the Purchaser may require a 338(h)(10) election be taken in lieu of a Conversion, in which event the Agreement will be revised accordingly. Simmons and Holdings shall take any reasonable action requested in writing by Purchaser, including taking a position on a Tax Return, to minimize the amount of Extra Taxes; provided that any such action that would have an adverse effect on either Simmons or Holdings in the reasonable good faith judgment of Simmons or Holdings shall be deemed not to constitute a reasonable action for purposes of this sentence. Purchaser shall have the right to review and comment on any Tax Return of Simmons or Holdings that reflects any Extra Taxes, and Simmons shall give good faith consideration to any such comments offered by Purchaser.

(d) Notwithstanding any other provisions hereof, if an audit or other proceeding is commenced, an adjustment is proposed, or any other claim is made by any Taxing Authority with respect to the Company (a “Tax Claim”) for a Pre-Closing Period or a Straddle Period, Purchaser shall (to the extent that it has been contacted by the Taxing Authority) promptly notify Simmons of such audit or other proceeding, proposed adjustment or claim. Simmons shall have the right to handle, defend, conduct and control any Tax Claim relating to a Pre-Closing Period. Simmons shall also have the right to compromise or settle any such Tax Claim for Pre-Closing Periods that it has the authority to control pursuant to the preceding sentence, provided any such settlement involving conduct or other equitable remedies shall be subject to Purchaser’s prior written approval; and provided further that, with respect to any Tax Claim involving Extra Taxes, (i) Simmons shall keep Purchaser reasonably informed and consult seriously and in good faith with Purchaser and its tax advisors with respect to any issue relating to such Extra Taxes, (ii) Simmons shall provide Purchaser with copies of all correspondence, notices and other written materials received from any Taxing Authorities and shall otherwise keep Purchaser and its tax advisors advised of significant developments in the Tax Claim with respect to such Extra Taxes and of significant communications involving representatives of the Taxing Authorities, and (iii) Simmons shall provide Purchaser with a copy of any written submission to be sent to a Taxing Authority relating to Extra Taxes prior to the submission thereof and shall give serious and good faith consideration to any comments or suggested revisions that Purchaser or its tax advisors may have with respect thereto. In the event Simmons settles or compromises any Tax Claim relating to a Pre-Closing Period which requires Purchaser to pay Extra Taxes without Purchaser’s consent (not to be unreasonably withheld), and Purchaser in good faith objects to the terms of such settlement or compromise with respect to the Extra Taxes, then Purchaser shall have the right to submit the matter to the Arbitrator. The Arbitrator shall determine within 30 days of the submission of the matter to it (which such determination shall be final and binding upon the parties) whether the settlement or compromise by Simmons with respect to Extra Taxes was reasonable with respect to the Extra Taxes that are as a result due. If the Arbitrator determines that such settlement or compromise was not reasonable with respect to the Extra Taxes that are as a result due, then Purchaser shall have no obligation to pay the Extra Taxes. Where a Tax Claim relates to a Straddle Period, both Simmons and Purchaser shall equally represent the Company, and shall jointly consent to any compromise or settlement, which consents shall not be unreasonably withheld. To the extent that Simmons requires a power of attorney to represent the Company before a Taxing Authority, Purchaser, the Company or any of their Affiliates (as appropriate), promptly upon written request by Simmons, shall execute such powers or specific authorizations of representative capacity, including acknowledgment on such power or authorization of Simmons’s settlement authority described in this Section 8.13(d). In the event of a conflict between the provisions of this Section 8.13(d), on the one hand, and the provisions of Section 10.4, on the other, the provisions of this Section 8.13(d) shall control.

(e) Any refunds (and any interest received thereon) of any Tax with respect to the Company attributable to a taxable period beginning after the Closing Date or the post-Closing portion of a Straddle Period shall belong to the Company. Any refunds (and any interest received thereon) of any Tax with respect to the Company attributable to a Pre-Closing Period or the pre-Closing portion of a Straddle Period shall belong to Simmons except for refunds attributable to Extra Taxes, which shall be paid to the Company net of any Taxes imposed on the receipt thereof.

(f) Following the Closing, Purchaser and Simmons shall provide each other with such assistance as may reasonably be requested by either of them in connection with the preparation of any Tax Return, any audit or other examination by any Taxing Authority, or any judicial or administrative proceedings relating to Liability for Taxes of the Company. The party requesting assistance hereunder shall reimburse the other for reasonable out-of-pocket expenses incurred in providing such assistance.

(g) Any and all Tax allocation or Tax sharing agreements between the Company on the one hand, and Simmons or any of its Affiliates on the other hand, shall be terminated as to the Company as of the Closing Date and, from and after the Closing Date, the Company shall not be obligated to make any payment pursuant to any such agreement for any past or future period.

8.14 Financing. Purchaser shall use commercially reasonable efforts to take, or cause to be taken, all actions and to do, or cause to be done, all things necessary, proper or advisable to arrange the Financing. In the event any portion of Financing becomes unavailable, Purchaser shall use commercially reasonable efforts to arrange to obtain alternative financing from alternative sources in an amount sufficient to consummate the transactions contemplated herein on terms not materially less beneficial to Purchaser as promptly as practicable following the occurrence of such event.

## CONDITIONS TO CLOSING

9.1 Conditions Precedent to Obligations of Purchaser. The obligation of Purchaser to consummate the transactions contemplated by this Agreement is subject to the fulfillment, on or prior to the Closing Date, of each of the following conditions (any or all of which may be waived by Purchaser in whole or in part to the extent permitted by applicable Law):

(a) the representations and warranties of the Company and Holdings set forth in this Agreement shall be true and correct at and as of the Closing, except to the extent such representations and warranties relate to an earlier date (in which case such representations and warranties shall be true and correct on and as of such earlier date); provided, however that, the representations and warranties set forth in Sections 5.1 and 5.4 shall instead be read as set forth on Schedule 9.1 hereto, and provided further however, that in the event of a breach of a representation or warranty, the condition set forth in this Section 9.1(a) shall be deemed satisfied unless the effect of any or all such breaches of representations and warranties result in a Material Adverse Effect, and Purchaser shall have received a certificate signed by an authorized officer of the Company, dated the Closing Date, to the foregoing effect;

(b) the Company and Holdings shall have performed and complied in all material respects with all obligations and agreements required by this Agreement to be performed or complied with by them on or prior to the Closing Date, and Purchaser shall have received a certificate signed by an authorized officer of the Company, dated the Closing Date, to the foregoing effect;

(c) there shall not be in effect any Order by a Governmental Body of competent jurisdiction restraining, enjoining or otherwise prohibiting the consummation of the transactions contemplated hereby;

(d) there shall not have been or occurred any event, change, occurrence or circumstance that, individually or in the aggregate with any such events, changes, occurrences or circumstances, has had a Material Adverse Effect since the Balance Sheet Date;

(e) the waiting period applicable to the transactions contemplated by this Agreement under the HSR Act shall have expired or early termination shall have been granted;

(f) Holdings and the Company shall have obtained at least 90% of the consents listed on Schedule 9.1(f) and copies thereof shall have been delivered to Purchaser; provided that such 90% shall include the 5 largest revenue producing (based on 2005 fiscal year revenues) stores;

(g) the Company shall have received the written resignations, effective as of the Closing Date, of such of the Managers and officers of the Company other than such officers of the Company who are Continuing Employees of the Company;

(h) Simmons shall have executed and delivered to Purchaser the Dealer Incentive Agreement substantially in the form of Exhibit C (the "Dealer Incentive Agreement");

(i) Simmons shall have executed and delivered to Purchaser (A) a new Authorized Dealer Agreement between The Sleep Train, Inc. or one of its Affiliates (which shall cover The Sleep Train, Inc. and the Company) and Simmons (the "Dealer Agreement") and (B) a new Co-op Advertising Agreement between The Sleep Train, Inc. or one of its Affiliates (which shall cover The Sleep Train, Inc. and the Company) and Simmons (the "Co-op Agreement"), in each case only to revise the existing forms of such agreements attached hereto as Exhibit E and Exhibit F, respectively, in order to make the termination provisions consistent with the termination provisions contained in the Dealer Incentive Agreement and to provide no greater rights for either party to terminate the Authorized Dealer Agreement or Co-op Agreement than set forth in the Dealer Incentive Agreement;

(j) Holdings shall have delivered, or caused to be delivered, to Purchaser certificates representing the Units, duly endorsed in blank or accompanied by separate assignment of units;

(k) all undischarged judgments and Liens (other than Permitted Exceptions) shall have been paid off in full and Purchaser shall have received copies of all pay-off letters in respect of all Closing Date Debt (or, with respect to any capitalized leases, at the election of Purchaser, assumed by Purchaser) and such other instruments evidencing the satisfaction and cancellation of such Closing Date Debt, including, without limitation, executed UCC-3 termination statements as reasonably requested by Purchaser;

(l) Holdings shall have delivered to Purchaser a statement certifying that it is not a foreign person within the meaning of Section 1445 of the Code;

(m) the Company shall deliver to the Purchaser an opinion of counsel for the Company, Holdings and Simmons, dated as of the Closing Date, in substantially the form of Exhibit D; and

(n) this Agreement and the consummation of the transactions completed hereunder shall have been approved by the Board of Directors or Managers of Company and Holdings, and each of Company and Holdings shall have delivered to Purchaser a copy of the resolutions of the Board of Directors and Managers, approving this Agreement and the transactions described herein, certified by each entity's respective Secretary.

9.2 Conditions Precedent to Obligations of Holdings and Simmons. The obligations of Holdings and Simmons to consummate the transactions contemplated by this Agreement are subject to the fulfillment, prior to or on the Closing Date, of each of the following conditions:

(a) the representations and warranties of Purchaser set forth in this Agreement shall be true and correct at and as of the Closing, except to the extent such representations and warranties relate to an earlier date (in which case such representations and warranties shall be true and correct on and as of such earlier date) and Holdings and Simmons shall have received a certificate signed by an authorized officer of Purchaser, dated the Closing Date, to the foregoing effect;

(b) Purchaser shall have performed and complied in all material respects with all obligations and agreements required by this Agreement to be performed or complied with by Purchaser on or prior to the Closing Date, and Holdings and Simmons shall have received a certificate signed by an authorized officer of Purchaser, dated the Closing Date, to the foregoing effect;

(c) there shall not be in effect any Order by a Governmental Body of competent jurisdiction restraining, enjoining or otherwise prohibiting the consummation of the transactions contemplated hereby;

(d) the waiting period applicable to the transactions contemplated by this Agreement under the HSR Act shall have expired or early termination shall have been granted;

(e) Purchaser shall have delivered, or caused to be delivered, to Holdings and Simmons evidence of the wire transfers referred to in Section 3.2 hereof;

(f) Purchaser shall have executed and delivered to Holdings and Simmons the Dealer Incentive Agreement;

(g) Purchaser shall have executed and delivered to Holdings and Simmons the Dealer Agreement;

(h) Purchaser shall have executed and delivered to Holdings and Simmons the Co-op Agreement; and

(i) this Agreement and the consummation of the transactions completed hereunder shall have been approved by the Board of Managers of Purchaser, and Purchaser shall have delivered to Simmons a copy of the resolutions of the Board of Managers, approving this Agreement and the transactions described herein, certified by Purchaser's Secretary.

### 9.3 Notices; Frustration of Closing Conditions.

(a) Each of the Company, Holdings and Simmons, on the one hand, and Purchaser, on the other hand, agree to give prompt notice to each other of, and to use reasonable efforts to remedy, (i) the occurrence or failure to occur of any event which occurrence or failure to occur would be likely to cause any of its or their representations or warranties in this Agreement to be untrue or inaccurate in any material respect at the Closing Date, and (ii) any material failure on its or their part to comply with or satisfy any covenant, condition or agreement to be complied with or satisfied by it or them hereunder; provided, however, that the delivery of any notice pursuant to this Section 9.3 shall not limit or otherwise affect the remedies available hereunder to the party receiving such notice.

(b) None of the Company, Purchaser, Holdings or Simmons may rely on the failure of any condition set forth in Sections 9.1 or 9.2, as the case may be, if such failure was caused by such party's (or its affiliates) failure to comply with any provision of this Agreement.

## ARTICLE X

### INDEMNIFICATION

#### 10.1 Survival of Representations and Warranties.

(a) The representations and warranties of the parties contained in this Agreement shall, subject to Section 10.5, survive the Closing and claims may be asserted with respect thereto to the extent permitted by this Article X.

(b) All of the covenants or other agreements of the parties contained in this Agreement shall survive until fully performed or fulfilled, unless and to the extent only that non-compliance with such covenants or agreements is waived in writing by the party entitled to such performance.

#### 10.2 Indemnification by Simmons.

(a) Subject to Sections 8.13 and 10.5 hereof, Simmons hereby agrees to indemnify and hold Purchaser, the Company, and their respective directors, officers, employees, Affiliates, stockholders, agents, attorneys, representatives, successors and permitted assigns (collectively, the "Purchaser Indemnified Parties") harmless from and against (without duplication) any and all losses, liabilities, claims, demands, judgments, damages, fines, suits, actions, costs and expenses including without limitation, interest, penalties, cost of investigation and defense, and reasonable attorneys' and other professional fees and expenses (individually, a "Loss" and, collectively, "Losses");

(i) based upon or resulting from the failure of any of the representations or warranties made by Simmons, Holdings or the Company in this Agreement to be true and correct in all respects at and as of the date hereof and at and as of the Closing Date, regardless of whether the Purchaser relied on the truth of such representation or warranty or had any knowledge of any breach thereof;

(ii) based upon or resulting from the breach or nonfulfillment of any covenant on the part of Simmons, Holdings or the Company;

(iii) except as provided in Sections 8.13(c) and 10.3(c) below, (A) based upon or resulting from any Taxes (including pursuant to any Tax Sharing, Tax Indemnity or Tax allocation agreement or arrangement) of the Company or any of its Affiliates with respect to any Pre-Closing Period or the pre-Closing portion of any Straddle Period (computed in accordance with Section 8.13(b)) (whether now or hereafter known or due upon audit or adjustment by any Governmental Body or otherwise) and (B) any Taxes for which Simmons is responsible under Section 11.1;

(iv) based upon or resulting from any Closing Date Debt;

(v) based upon or resulting from (A) any undischarged judgments existing as of the Closing or (B) any Liens existing as of the Closing (other than Permitted Exceptions); and

(vi) based upon or resulting from any restricted stock agreement, registration rights agreement, securityholders' agreement, or other similar Contract relating to equity or phantom equity incentive compensation to which any employee is a party or is subject, including any such type of Contract between any employee and Simmons Company, a Delaware corporation, Simmons or any of their respective Affiliates.

(b) Purchaser acknowledges that Simmons shall not be liable for any Losses or Liabilities arising out of or relating to the failure to obtain the consent of any party under any Contract to the consummation of the transactions contemplated hereby if Purchaser closes the transactions contemplated hereunder without such consent being obtained.

#### 10.3 Indemnification by Purchaser. Subject to Section 10.5, Purchaser hereby agrees to indemnify and hold Holdings or Simmons and their respective directors, officers,

employees, Affiliates, stockholders, agents, attorneys, representatives, successors and permitted assigns (collectively, the “Simmons Indemnified Parties”) harmless from and against, and pay to the applicable Simmons Indemnified Parties the amount of, any and all Losses:

- (a) based upon or resulting from the failure of any of the representations or warranties made by Purchaser in this Agreement to be true and correct in all respects at the date hereof and as of the Closing Date;
- (b) based upon or resulting from the breach or nonfulfillment of any covenant on the part of Purchaser; and
- (c) any Taxes for which Purchaser is responsible under Section 8.13 or 11.1.

#### 10.4 Indemnification Procedures.

- (a) A claim for indemnification for any matter not involving a third-party claim may be asserted by notice to the party from whom indemnification is sought.
- (b) Subject to Section 8.13(d), which shall control with respect to Tax Claims for Pre-Closing Periods or the pre-Closing portion of Straddle Periods, if any Legal Proceeding shall be instituted, or any claim shall be asserted, by any Person that is not a party (or an Affiliate of a party) hereto as to which indemnification may be sought by any Purchaser Indemnified Party under Section 10.2 or any Simmons Indemnified Party under Section 10.3 hereof (regardless of the limitations set forth in Section 10.5) (an “Indemnification Claim”), the Purchaser Indemnified Party or the Simmons Indemnified Party, as applicable (each, an “Indemnified Party”), shall promptly cause written notice of the assertion of any Indemnification Claim of which it has knowledge to be forwarded to the other party (the “Indemnifying Party”). The failure of the Indemnified Party to give reasonably prompt notice of any Indemnification Claim shall not release, waive or otherwise affect the Indemnifying Party’s obligations with respect thereto except to the extent that the Indemnifying Party is prejudiced as a result of such failure. The Indemnifying Party shall have the right, at its expense, to be represented by counsel of its choice, which must be reasonably satisfactory to the Indemnified Party, and to defend against, negotiate, settle or otherwise deal with any Indemnification Claim which relates to any Losses indemnified against by it hereunder. If the Indemnifying Party elects to defend against, negotiate, settle or otherwise deal with any Indemnification Claim, it shall within 30 days (or sooner, if the nature of the Indemnification Claim so requires) notify the Indemnified Party whether or not it shall do so; provided that the attorneys’ fees and other Losses incurred by the Indemnifying Party in connection with such defense, negotiation, settlement or other dealings shall not reduce the amount recoverable under the Cap by the Indemnified Parties. If the Indemnifying Party elects not to defend against, negotiate, settle or otherwise deal with any Indemnification Claim which relates to any Losses indemnified against hereunder, the Indemnified Party may defend against, negotiate, settle or otherwise deal with such Indemnification Claim, and the Indemnifying Party shall promptly, and in any event within 20 days after demand therefor, reimburse the Indemnified Party for the reasonable costs and expenses of such defense, including attorneys’ fees and other Losses incurred by the Indemnified Party in connection therewith. If the Indemnifying Party shall assume the defense of any Indemnification Claim, the Indemnified Party may participate, at his or its own expense, in the defense of such Indemnification Claim; provided, however, that such Indemnified Party shall be entitled to participate in any such defense with separate counsel at the expense (so long as such fees and expenses are reasonable) of the Indemnifying Party if, (i) so requested by the Indemnifying Party to participate or (ii) in the reasonable opinion of counsel to the Indemnified Party, a conflict or potential conflict exists between the Indemnified Party and the Indemnifying Party that would make such separate representation advisable; provided, further, that the Indemnifying Party shall not be required to pay for more than one such counsel (plus any appropriate local counsel) for all Indemnified Parties in connection with any Indemnification Claim. The parties hereto agree to cooperate fully with each other in connection with the defense, negotiation or settlement of any such Indemnification Claim, and the party assuming the defense of any Indemnification Claim shall keep the other party reasonably informed at all times of the progress and development of its defense of and compromise efforts with respect to such Indemnification Claim and shall furnish the other party with copies of all relevant pleadings, correspondence and other documents. Notwithstanding anything in this Section 10.4 to the contrary, neither the Indemnifying Party nor the Indemnified Party shall, without the written consent of the other party, settle or compromise any Indemnification Claim or permit a default or consent to entry of any judgment unless (i) the claimant and such party provide to such other party an unqualified release from all liability in respect of the Indemnification Claim and (ii) the settlement, compromise, or judgment involves only the payment of money damages by the Indemnifying Party and does not impose an injunction or other equitable relief on the Indemnified Party or impose any restrictions on the operation of the business of the Indemnified Party or its Affiliates, in which case the consent of the other party shall not be unreasonably withheld or delayed.
- (c) After any final decision, judgment or award shall have been rendered by a Governmental Body of competent jurisdiction and the expiration of the time in which to appeal therefrom, or a settlement shall have been consummated, or the Indemnified Party and the Indemnifying Party shall have arrived at a mutually binding agreement with respect to an Indemnification Claim hereunder, the Indemnified Party shall forward to the Indemnifying Party notice of any Losses and other sums due and owing by the Indemnifying Party pursuant to this Agreement with respect to such matter.

(d) Any amount due and payable hereunder shall accrue interest from and after the date due until paid in full at the “prime” rate, as announced by The Wall Street Journal, Eastern Edition, in effect as of the date payment first became due, calculated based on a 365-day year and the actual number of days elapsed.

#### 10.5 Certain Limitations on Indemnification.

- (a) Notwithstanding the provisions of this Article X, neither Simmons nor Purchaser shall have any indemnification obligations for Losses under Sections 10.2(a)(i) and 10.2(a)(ii) or Sections 10.3(a) and 10.3(b), for any individual item, or group of items arising out of the same event, unless the aggregate amount of all such Losses exceeds \$450,000 (the “Basket”) and then only for Losses in excess of the Basket. In no event shall the aggregate indemnification to be paid by Simmons or Purchaser under this Article X exceed \$12,000,000 (the “Cap”). Notwithstanding the foregoing, neither the Basket nor the Cap shall apply to Losses based upon or related to (i) fraud, criminal wrongdoing or willful breach, (ii) any matter subject to indemnification pursuant to Sections 10.2(a)(iii) through 10.2(a)(vi), or (iii) the failure to be true and correct of any of the representations and warranties set forth in Section 5.1 (Organization), 5.2 (Authorization), 5.4 (Capitalization), 5.9 (Taxes), 5.14(e) through 5.14(j) (Employee Benefit Plans), 5.15(c)(ii) - 5.15(c)(iv), 6.1 (Organization), 6.2 (Authorization), 6.4 (Ownership), 6.6 (Financial Advisors), 7.1 (Organization), 7.2 (Authorization) or 7.6 (Financial Advisors) hereof.
- (b) No Indemnifying Party shall be required to indemnify the Indemnified Party to the extent of any Losses that a court of competent jurisdiction shall have determined by final judgment to have resulted from the bad faith, gross negligence or willful misconduct of the Indemnified Party.
- (c) The indemnification obligations set forth in this Article X with respect to a breach of a particular representation, warranty, agreement or covenant shall survive the Closing for a period of 21 months from the Closing Date; provided, however, that Simmons’ obligation to indemnify the Purchaser for any Losses based upon or related to (i) fraud, criminal wrongdoing or willful breach, (ii) any matter subject to indemnification pursuant to Sections 10.2(a)(iii) through 10.2(a)(vi), or (iii) the failure to be true and correct of any of the representations and warranties set forth in Sections 5.2 (Authorization), 5.4 (Capitalization), 5.9 (Taxes) and 6.4 (Ownership) shall survive the Closing Date until expiration of the applicable statute of limitations.
- (d) Absent fraud, Purchaser shall not make any claim for indemnification under this Article X in respect of any matter that is taken into account in the calculation of any adjustment to the Purchase Price pursuant to Section 3.3.

## 10.6 Calculation of Losses; Materiality.

(a) The amount of any Losses for which indemnification is provided under this Article X shall be net of any Tax benefit actually recognized or any other amounts actually recovered by the Indemnified Party from any other Person with respect thereto; provided, however, that each Indemnifying Party waives any right to require any Indemnified Party to (i) recover under any insurance policies for any Losses, (ii) proceed against any other Person, or (iii) pursue any other remedy whatsoever in the power of any Purchaser Indemnified Party. An Indemnified Party shall not be entitled to any right of set-off against any payment due the Indemnifying Party for any Losses to which any Indemnified Party is entitled to be indemnified hereunder with respect to any Indemnification Claim unless (i) the Indemnifying Party has agreed in writing it is obligated to pay the amount of the Losses which the Indemnified Party seeks to set-off, or (ii) a judgment has been rendered by a court of competent jurisdiction that the Indemnifying Party owes the Indemnified Party the amount of the Losses which the Indemnified Party seeks to set-off.

(b) Materiality; Material Adverse Effect. For purposes of determining whether a representation or warranty has been breached for purposes of indemnification under this Article X, the words “material” and “Material Adverse Effect” or variations thereof shall be disregarded, and the phrase “resulting in Liabilities or Losses in excess of \$75,000 individually or \$150,000 in the aggregate” (or substantially similar variations thereof) shall as a measure of materiality, also be disregarded.

10.7 Tax Treatment of Indemnity Payments. Simmons and Purchaser agree to treat any indemnity payment made pursuant to this Article X as an adjustment to the Purchase Price for federal, state, local and foreign income Tax purposes.

10.8 Exclusive Remedy. From and after the Closing, the sole and exclusive remedy for any breach or failure to be true and correct, or alleged breach or failure to be true and correct, of any representation or warranty or any covenant or agreement in this Agreement, shall be indemnification in accordance with this Article X, except with respect to claims resulting from fraud, criminal wrongdoing or willful breach. In furtherance of the foregoing, the parties hereby waive, to the fullest extent permitted by applicable Law, any and all other rights, claims and causes of action (including rights of contributions, if any) known or unknown, foreseen or unforeseen, which exist or may arise in the future, that it may have against Holdings, Simmons or Purchaser, as the case may be, arising under or based upon any federal, state or local Law (including any such Law relating to environmental matters or arising under or based upon any securities Law, common Law or otherwise). Notwithstanding the foregoing, this Section 10.9 shall not operate to interfere with or impede the operation of the provisions of Article III providing for the (i) resolution of certain disputes relating to the Purchase Price between the parties and/or by the Arbitrator and (ii) limit the rights of the parties to seek equitable remedies (including specific performance or injunctive relief), including under Section 8.11.

## ARTICLE XI

### MISCELLANEOUS

11.1 Payment of Sales, Use or Similar Taxes. All sales, use, transfer, intangible, recordation, documentary stamp or similar Taxes or charges, of any nature whatsoever (collectively, the “Transfer Taxes”), applicable to, or resulting from, the transactions contemplated by this Agreement shall be borne 50% by Simmons and 50% by Purchaser; provided, however, that Purchaser shall be responsible for any and all Transfer Taxes resulting from the consummation of the transactions contemplated by this Agreement (including, without limitation, the Conversion) which Taxes would not have arisen had the transaction been structured as a transfer of stock of a corporation to the Purchaser in a transaction pursuant to which an election under Section 338(h)(10) of the Code had been made; provided, further, it is acknowledged and agreed by the parties that Purchaser shall not be responsible for any Transfer Taxes arising out of the transfer of real property or improvements thereon.

11.2 Expenses. Except as otherwise provided in this Agreement, each of Holdings and Simmons (with respect to their and the Company’s expenses) and Purchaser shall bear its own expenses incurred in connection with the negotiation and execution of this Agreement and each other agreement, document and instrument contemplated by this Agreement and the consummation of the transactions contemplated hereby and thereby; provided, however, that Purchaser shall bear all pre-Closing expenses related to the Conversion, including obtaining consents from the Board of Directors and the sole stockholder of the Company and the filing of a certificate of conversion with the Delaware Secretary of State (which shall be performed by Simmons or its counsel) and obtaining or seeking to obtain any rulings requested by Purchaser from any Taxing Authorities with respect to the Conversion (which shall be performed by Purchaser or its counsel), as well as any post-Closing expenses related to the Conversion, including filing fees or other costs and expenses associated with assigning Intellectual Property and filing notices of name changes with any Governmental Body (which shall be performed by Purchaser or its counsel). Purchaser shall be responsible for all filing fees required in connection with compliance with the HSR Act.

## 11.3 Submission to Jurisdiction; Consent to Service of Process.

(a) The parties hereto hereby irrevocably submit to the non-exclusive jurisdiction of any federal or state court located within Seattle, Washington over any dispute arising out of or relating to this Agreement or any of the transactions contemplated hereby and each party hereby irrevocably agrees that all claims in respect of such dispute or any suit, action proceeding related thereto may be heard and determined in such courts. The parties hereby irrevocably waive, to the fullest extent permitted by applicable law, any objection which they may now or hereafter have to the laying of venue of any such dispute brought in such court or any defense of inconvenient forum for the maintenance of such dispute. Each of the parties hereto agrees that a judgment in any such dispute may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law.

(b) Each of the parties hereto hereby consents to process being served by any party to this Agreement in any suit, action or proceeding by the delivery of a copy thereof in accordance with the provisions of Section 11.7.

11.4 Entire Agreement; Amendments and Waivers. This Agreement (including the schedules and exhibits hereto) and the Confidentiality Agreement represent the entire understanding and agreement between the parties hereto with respect to the subject matter hereof and thereof. This Agreement can be amended, supplemented or changed, and any provision hereof can be waived, only by written instrument making specific reference to this Agreement signed by the party against whom enforcement of any such amendment, supplement, modification or waiver is sought. No action taken pursuant to this Agreement, including any investigation by or on behalf of any party, shall be deemed to constitute a waiver by the party taking such action of compliance with any representation, warranty, covenant or agreement contained herein. The waiver by any party hereto of a breach of any provision of this Agreement shall not operate or be construed as a further or continuing waiver of such breach or as a waiver of any other or subsequent breach. No failure on the part of any party to exercise, and no delay in exercising, any right, power or remedy hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of such right, power or remedy by such party preclude any other or further exercise thereof or the exercise of any other right, power or remedy.

11.5 Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware applicable to contracts made and performed in such State without giving effect to the choice of law principles of such State that would require or permit the application of the laws of another jurisdiction.

11.6 Notices. All notices and other communications under this Agreement shall be in writing and shall be deemed given (i) when delivered personally by hand (with written confirmation of receipt), (ii) when sent by facsimile (with written confirmation of transmission) or (iii) one business day following the day sent by overnight courier (with

written confirmation of receipt), in each case at the following addresses and facsimile numbers (or to such other address or facsimile number as a party may have specified by notice given to the other party pursuant to this provision):

If to Holdings or Simmons, to:

c/o Simmons Bedding Company  
One Concourse Parkway, Suite 800  
Atlanta, GA 30328  
Facsimile: (770) 206-2669  
Attention: Chief Financial Officer and General Counsel

With copies (which shall not constitute notice) to:

Thomas H. Lee Partners, L.P.  
100 Federal Street, 35th Floor  
Boston, MA 02110  
Facsimile: (617) 227-3514  
Attention: Scott Schoen  
                  Todd Abbrecht  
                  George Taylor

and

Weil, Gotshal & Manges LLP  
  
100 Federal Street, 34th Floor  
  
Boston, MA 02110  
  
Facsimile: (617) 772-8333  
  
Attention: Marilyn French, Esq.

If to Purchaser, to:

ST San Diego, LLC  
  
8391 Auburn Boulevard  
  
Citrus Heights, CA 95610  
  
Facsimile: (916) 735-1382  
  
Attention: Dale Carlsen

With a copy to:

Shartsis Friese LLP  
  
One Maritime Plaza, 18th Floor  
  
San Francisco, CA 94111  
  
Facsimile: (415) 421-2922  
  
Attention: Derek Wilson, Esq.

11.7 Severability. If any term or other provision of this Agreement is invalid, illegal, or incapable of being enforced by any law or public policy, all other terms or provisions of this Agreement shall nevertheless remain in full force and effect so long as the economic or legal substance of the transactions contemplated hereby is not affected in any manner materially adverse to any party. Upon such determination that any term or other provision is invalid, illegal, or incapable of being enforced, the parties hereto shall negotiate in good faith to modify this Agreement so as to effect the original intent of the parties as closely as possible in an acceptable manner in order that the transactions contemplated hereby are consummated as originally contemplated to the greatest extent possible.

11.8 Binding Effect; Assignment. This Agreement shall be binding upon and inure to the benefit of the parties and their respective successors and permitted assigns. Nothing in this Agreement shall create or be deemed to create any third party beneficiary rights in any person or entity not a party to this Agreement except as provided below. No assignment of this Agreement or of any rights or obligations hereunder may be made by either Holdings, Simmons or Purchaser, directly or indirectly (by operation of law or

otherwise), without the prior written consent of the other parties hereto and any attempted assignment without the required consents shall be void. No assignment of any obligations hereunder shall relieve the parties hereto of any such obligations. Upon any such permitted assignment, the references in this Agreement to Purchaser shall also apply to any such assignee unless the context otherwise requires.

11.9 Non-Recourse. Excluding fraud or criminal wrongdoing, no past, present or future director, officer, employee, incorporator, member, partner, stockholder, Affiliate, agent, attorney or representative of Holdings, Simmons or the Company or any of their respective Affiliates shall have any liability for any obligations or liabilities of Holdings, Simmons or the Company under this Agreement of or for any claim based on, in respect of, or by reason of, the transactions contemplated hereby and thereby.

11.10 Counterparts. This Agreement may be executed in one or more counterparts, each of which will be deemed to be an original copy of this Agreement and all of which, when taken together, will be deemed to constitute one and the same agreement.

**\*\* REMAINDER OF PAGE INTENTIONALLY LEFT BLANK \*\***

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IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed by their respective authorized officers, as of the date first written above.

ST SAN DIEGO, LLC

By: /s/ Dale R. Carlsen  
Name: Dale R. Carlsen  
Title: Managing Member

SLEEP COUNTRY USA, INC.

By: /s/ William S. Creekmuir  
Name: William S. Creekmuir  
Title: Executive Vice President, Assistant Treasurer and Assistant Secretary

SC HOLDINGS, INC.

By: /s/ William S. Creekmuir  
Name: William S. Creekmuir  
Title: Executive Vice President, Assistant Treasurer and Assistant Secretary

SIMMONS BEDDING COMPANY

By: /s/ Charles R. Eitel  
Name: Charles R. Eitel  
Title: Chief Executive Officer

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## Guarantee

The Sleep Train, Inc., a California corporation ("Sleep Train") and an affiliate of the Purchaser, hereby guarantees to Simmons the payment and performance of all obligations and covenants of Purchaser under this Unit Purchase Agreement dated as of July 24, 2006 among ST San Diego, LLC, Sleep Country USA, Inc., SC Holdings, Inc. and Simmons Bedding Company (the "Agreement"), it being acknowledged that Simmons need not exhaust its remedies against Purchaser in order to enforce this guarantee. Capitalized terms used herein but not defined shall have the meanings set forth in the Agreement.

Sleep Train hereby represents and warrants (and agrees to indemnify Simmons for any losses arising out of any breach of such representation and warranties) to Simmons the following:

1. Organization and Good Standing. Sleep Train is a corporation duly organized, validly existing and in good standing under the laws of the State of California and has all requisite limited liability power and authority to own, lease and operate properties and carry on its business.

2. Authorization of Guarantee. Sleep Train has full corporate power and authority to execute and deliver this Guarantee and to perform its obligations hereunder. The execution, delivery and performance by Sleep Train of this Guarantee have been duly authorized by all necessary limited liability company action on behalf of Sleep Train. This Guarantee has been duly executed and delivered by Sleep Train and this Guarantee constitutes the legal, valid and binding obligation of Sleep Train, enforceable against Sleep Train in accordance with its terms, subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors' rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity).

3. Conflicts; Consents of Third Parties.

(a) None of the execution, delivery and performance by Sleep Train of this Guarantee will conflict with, or result in any violation of or default (with or without notice or lapse of time, or both) under, or give rise to a right of termination or cancellation under, any provision of (i) the certificate of incorporation or by-laws of Sleep Train; (ii) any Contract or Permit to which Sleep Train is a party or by which Sleep Train or its properties or assets are bound; (iii) any Order of any Governmental Body applicable to Sleep Train or by which any of the properties or assets of Sleep Train are bound; or (iv) any applicable Law.

(b) No consent, waiver, approval, Order, Permit or authorization of, or declaration or filing with, or notification to, any Person or Governmental Body is required on the part of Sleep Train in connection with the execution and delivery of this Guarantee or the performance of its obligations hereunder.

4. Litigation. There are no Legal Proceedings pending or, to the actual knowledge of Sleep Train (without any docket or other electronic search having been conducted) threatened, that are reasonably likely to prohibit or restrain the ability of Sleep Train to enter into this Guarantee or perform its obligations hereunder.

This Guarantee shall be governed by and construed in accordance with the laws of the State of Delaware applicable to contracts made and performed in such State without giving effect to the choice of law principles of such State that would require or permit the application of the laws of another jurisdiction.

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THE SLEEP TRAIN, INC.

By: /s/ Dale R. Carlsen

Name: Dale R. Carlsen

Title: President

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### **Schedule 1**

“Adjusted EBITDA” means the earnings before interest, income taxes, depreciation and amortization of the Company (“EBITDA”), but including to the extent not already added or deducted in EBITDA, (a) as an add-back, that portion of the annual management fee payable by the Company to Simmons equal to (i) the total management fee for the last full 12-month period ended on July 1, 2006 less (ii) \$115,000, representing that portion of the fee attributable to recurring costs of the Company (e.g., audits fees, insurance and tax preparation), (b) as add-backs, any bonus expense for Senior Executives for that portion of the 2005 fiscal year from January 1, 2005 through June 30, 2005 as if bonuses for 2005 were accrued in 12 equal installments during the year, (c) as deductions, bonus expense for Senior Executives as if the anticipated bonus expense for such executives for that portion of the 2006 fiscal year up to and including the Closing Date (based on the Company’s projection’s for bonus expense for fiscal year 2006) were accrued in 12 equal installments during the year, (d) as a deduction, \$20,000 relating to equity incentive compensation, (e) as a deduction, \$100,000 relating to Simmons’ one-time rebate fees, and (f) as add-backs, business and occupation taxes.

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**Exhibit A**

**Closing Date Working Capital Statement**

A Closing Date Working Capital Statement will be provided prior to Closing (the Preliminary Closing Date Working Capital Statement), at Closing (the Estimated Working Capital Statement) and post-Closing (the Actual Closing Date Working Capital Statement) pursuant to Article III.

Closing Date Current Assets include the sum of the following items (\$ in thousands):

Cash \$  
Accounts Receivable, Net of Allowances \$  
Co-op Receivable \$  
Inventory \$  
Prepays & Short Term Deposits \$  
TOTAL CURRENT ASSETS \$

LESS:

Closing Date Current Liabilities includes the sum of the following items (\$ in thousands):

Accounts Payable \$  
Accrued Liabilities \$  
Customer Deposits \$  
Salaries, Wages, Commissions &  
Bonuses Payable \$  
Benefits & Payroll Taxes Payable \$  
401(k) Profit Sharing Contribution \$  
State Sales and Local Taxes \$  
Intercompany Liabilities, Net \$  
TOTAL CURRENT LIABILITIES \$

EQUALS:

**WORKING CAPITAL \$ \_\_\_\_\_**