
**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 June 25, 2005

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 333-113861

SIMMONS BEDDING COMPANY

(Exact name of registrant as specified in its charter)

Delaware

13-3875743

(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 an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes No

The number of shares of the registrant's common stock outstanding as of August 9, 2005 was 100.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

Simmons Bedding Company and Subsidiaries

Unaudited Condensed Consolidated Statements of Operations and Comprehensive Income

(In thousands)

	Quarter Ended		Six Months Ended	
	June 25, 2005	June 26, 2004	June 25, 2005	June 26, 2004
Net sales	\$208,042	\$201,795	\$413,624	\$425,115
Cost of products sold	<u>117,256</u>	<u>110,245</u>	<u>231,422</u>	<u>230,110</u>
Gross profit	<u>90,786</u>	<u>91,550</u>	<u>182,202</u>	<u>195,005</u>
Operating expenses:				
Selling, general and administrative expenses	73,056	73,605	152,126	158,866
Plant closure charges	40	764	40	764
Amortization of intangibles	1,417	(1,197)	2,858	2,289
Transaction expenses	177	662	177	662
Licensing fees	<u>(2,815)</u>	<u>(2,481)</u>	<u>(4,866)</u>	<u>(5,062)</u>
	<u>71,875</u>	<u>71,353</u>	<u>150,335</u>	<u>157,519</u>
Operating income	18,911	20,197	31,867	37,486
Interest expense, net	<u>13,203</u>	<u>10,888</u>	<u>25,392</u>	<u>21,981</u>
Income before income taxes	5,708	9,309	6,475	15,505
Income tax expense	<u>2,029</u>	<u>3,351</u>	<u>2,313</u>	<u>5,582</u>
Net income	3,679	5,958	4,162	9,923
Other comprehensive income:				
Foreign currency translation adjustment	<u>(9)</u>	<u>(8)</u>	<u>(6)</u>	<u>(10)</u>
Comprehensive income	<u>\$ 3,670</u>	<u>\$ 5,950</u>	<u>\$ 4,156</u>	<u>\$ 9,913</u>

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

Simmons Bedding Company and Subsidiaries

Condensed Consolidated Balance Sheets

(Dollars in thousands)

	June 25, 2005 <u>(Unaudited)</u>	December 25, 2004* <u></u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 31,368	\$ 23,854
Accounts receivable, less allowances for doubtful receivables, discounts and returns of \$5,024 and \$5,131	71,915	85,433
Inventories	32,482	33,300
Deferred income taxes	1,448	2,445
Other current assets	<u>17,893</u>	<u>20,204</u>
Total current assets	<u>155,106</u>	<u>165,236</u>
Property, plant and equipment, net	60,034	62,842
Goodwill	492,560	488,686
Intangible assets, net	540,125	542,983
Other assets	<u>38,800</u>	<u>41,987</u>
	<u>\$1,286,625</u>	<u>\$1,301,734</u>

* Derived from the Company's 2004 audited Consolidated Financial Statements.

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

Simmons Bedding Company and Subsidiaries

Condensed Consolidated Balance Sheets

(Dollars in thousands)

	June 25, 2005 <u>(Unaudited)</u>	December 25, 2004* <u></u>
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current liabilities:		
Current maturities of long-term debt	\$ 839	\$ 4,124
Accounts payable	51,652	54,380
Accrued liabilities	<u>56,132</u>	<u>68,977</u>
Total current liabilities	<u>108,623</u>	<u>127,481</u>
Non-current liabilities:		
Long-term debt	746,474	748,015
Deferred income taxes	155,655	154,775
Other	<u>11,110</u>	<u>10,856</u>
Total liabilities	<u>1,021,862</u>	<u>1,041,127</u>
Commitments and contingencies		
Common stockholder's equity:		
Common stock, \$.01 par value; 3,000 shares authorized; 100 issued and outstanding	1	1
Additional paid-in capital	243,052	243,052
Retained earnings	21,586	17,424
Accumulated other comprehensive income	<u>124</u>	<u>130</u>
Total common stockholder's equity	<u>264,763</u>	<u>260,607</u>
	<u>\$1,286,625</u>	<u>\$1,301,734</u>

* Derived from the Company's 2004 audited Consolidated Financial Statements.

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

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

	Six Months Ended	
	June 25, 2005	June 26, 2004
Cash flows from operating activities:		
Net income	\$ 4,162	\$ 9,923
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13,121	10,719
Provision for bad debts, net	(107)	2,542
Provision for deferred income taxes	1,299	4,274
Non-cash interest expense	1,172	908
Non-cash stock compensation expense	—	3,308
Net changes in operating assets and liabilities:		
Accounts receivable	13,625	(11,553)
Inventories	818	3,108
Other current assets	2,311	5,774
Accounts payable	(2,728)	7,616
Accrued liabilities	(12,804)	6,689
Other, net	(2,321)	(5,110)
 Net cash provided by operating activities	 <u>18,548</u>	 <u>38,198</u>
Cash flows from investing activities:		
Purchases of property, plant and equipment	(2,586)	(6,728)
Proceeds from the sale of Gallery Corp., net	—	6,495
Purchase of certain assets of Simmons Juvenile Products, Inc.	(3,337)	—
Other, net	—	105
 Net cash used in investing activities	 <u>(5,923)</u>	 <u>(128)</u>
Cash flows from financing activities:		
Proceeds from (payments to) affiliate, net	(279)	925
Payments of senior credit facility, net	(4,668)	(11,675)
Payments of other debt	(158)	(6,002)
Payments of financing fees	—	(601)
 Net cash used in financing activities	 <u>(5,105)</u>	 <u>(17,353)</u>
 Net effect of exchange rate changes on cash	 <u>(6)</u>	 <u>(10)</u>
 Change in cash and cash equivalents	 7,514	 20,707
Cash and cash equivalents, beginning of period	<u>23,854</u>	<u>3,670</u>
 Cash and cash equivalents, end of period	 <u>\$ 31,368</u>	 <u>\$ 24,377</u>

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

Simmons Bedding Company and Subsidiaries
Consolidated Statement of Changes in Stockholder's Equity
(Dollars in thousands)

	Common Shares	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholder's Equity
December 25, 2004 (audited)	100	\$ 1	\$243,052	\$17,424	\$ 130	\$ 260,607
Net income	—	—	—	4,162	—	4,162
Other comprehensive income:						
Change in foreign currency translation	—	—	—	—	(6)	(6)
Comprehensive income (loss)				4,162	(6)	4,156
June 25, 2005 (unaudited)	100	\$ 1	\$243,052	\$21,586	\$ 124	\$ 264,763

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

A. Basis of Presentation

For purposes of this report, the “Company” refers to Simmons Bedding Company and its subsidiaries, collectively. These interim condensed consolidated financial statements of the Company are unaudited, and have been prepared in accordance with accounting principles generally accepted in the United States of America (“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 June 25, 2005, 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 25, 2004. Operating results for the periods ended June 25, 2005 are not necessarily indicative of future results that may be expected for the fiscal year ending December 31, 2005 or for any future period.

The Company operates on a 52/53 week fiscal year ending on the last Saturday in December. Fiscal year 2005 is a 53 week year, whereas fiscal year 2004 was a 52 week year. The fourth quarter of fiscal year 2005 will be comprised of 14 weeks, whereas each of the first, second and third quarters are comprised of 13 weeks.

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.

Certain amounts previously reported in the 2004 consolidated financial statements and related footnotes have been reclassified to conform to the current year presentation.

B. Inventories

A summary of inventories follows (in thousands):

	June 25, 2005	December 25, 2004
Raw materials	\$17,419	\$ 18,135
Work-in-progress	1,049	1,236
Finished goods	9,577	9,934
Inventory held at retail stores	<u>4,437</u>	<u>3,995</u>
	<u>\$32,482</u>	<u>\$ 33,300</u>

C. Acquisitions and Dispositions

In December 2003, THL Bedding Company, a wholly owned subsidiary of THL Bedding Holding Company (now known as Simmons Company) and an affiliate of Thomas H. Lee Partners, L.P., acquired Simmons Holdings, Inc. for approximately \$1.115 billion, including

related acquisition costs (the “Acquisition”). Concurrently with the closing of this transaction on December 19, 2003, each of THL Bedding Company and the operating company of Simmons Holdings, Inc., then named Simmons Company, merged with and into Simmons Holdings, Inc. with Simmons Holdings, Inc. continuing as the surviving corporation (now known as Simmons Bedding Company).

The Company sold its Gallery Corp. (“Mattress Gallery”) retail operations in a stock transaction on May 1, 2004 to Pacific Coast Mattress, Inc. (“PCM”) for cash proceeds of \$6.3 million plus the cancellation of all intercompany debt with the exception of current trade payables owed by Mattress Gallery to the Company. The cancellation of intercompany debt was recorded as a capital contribution to Mattress Gallery. No gain or loss was recorded on the sale since Mattress Gallery was recorded at fair value in connection with the Acquisition. As of June 25, 2005, the Company continued to guarantee approximately \$1.3 million of Mattress Gallery’s obligations under certain store leases that expire over various periods through 2010. The Company does not record a liability for this obligation on the condensed consolidated balance sheet. In connection with the sale, the Company entered into a supply agreement through April 2009 with PCM.

Prior to the sale of Mattress Gallery, the Company did not reflect Mattress Gallery’s results of operations as discontinued operations since the Company has an ongoing interest in the cash flows of the operations through the long-term supply agreement. For the quarter ended June 26, 2004, Mattress Gallery’s net sales and net loss were \$3.0 million and \$(0.9) million, respectively. For the six months ended June 26, 2004, Mattress Gallery’s net sales and net loss were \$12.9 million and \$(3.3) million, respectively.

On August 27, 2004, one of the Company’s then current subsidiaries, Simmons Juvenile Company, LLC (“Simmons Juvenile”), acquired certain assets and liabilities of the crib mattress and related soft goods business of Simmons Juvenile Products Company, Inc. (“Simmons Juvenile, Inc.” or “the Seller”), a then-current licensee of the Company, for \$19.7 million in cash, including transaction costs (the “Juvenile Acquisition”), plus contingent consideration based on Simmons Juvenile’s operating performance for the six months ended February 2005. The Company paid \$3.3 million of contingent consideration in the second quarter of 2005 and adjusted the purchase price allocation by such payment. On May 3, 2005, Simmons Juvenile merged with and into The Simmons Manufacturing Co., LLC, with The Simmons Manufacturing Co., LLC continuing as the surviving corporation.

Simmons Juvenile, Inc. manufactured and sold Simmons branded crib mattresses and related soft goods to the U.S. infant market. The Juvenile Acquisition provides the Company access to the U.S. infant market.

The Company recorded the Juvenile Acquisition using the purchase method of accounting and, accordingly, the purchase price has been allocated to the assets acquired and liabilities assumed based on their estimated fair market values. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed as of the date of the acquisition, adjusted for the contingent consideration paid in 2005 (in thousands):

Current assets	\$ 3,665
Property, plant and equipment	23
Goodwill	4,034
Intangibles	<u>18,000</u>
Total assets acquired	<u>25,722</u>
Current liabilities	(2,476)
Non-current liabilities	<u>(224)</u>
Total liabilities assumed	<u>(2,700)</u>
Purchase price	<u>\$ 23,022</u>

The intangible assets acquired include non-contractual customer agreements of \$8.8 million and trademarks of \$9.2 million. The non-contractual customer agreements have a weighted average life of eleven years. The trademarks have an indefinite life. The goodwill was assigned to the Company's wholesale segment. The tax-deductible goodwill was \$6.3 million and is expected to be deductible for tax purposes over 15 years. The tax benefit associated with the excess of tax-deductible goodwill over the reported amount of goodwill will be recognized when realized on the Company's tax return and will reduce the reported amount of goodwill associated with the Juvenile Acquisition. There were no pre-acquisition contingencies related to the Juvenile Acquisition.

The Juvenile Acquisition is not considered significant to the Company's balance sheets and statements of operations; therefore, pro forma information has not been presented.

D. Goodwill

The changes in the carrying amount of goodwill for the quarter and six months ended June 25, 2005 are as follows (in thousands):

	Wholesale Bedding	Retail	Consolidated
Balance as of December 25, 2004	\$476,394	\$12,292	\$ 488,686
Juvenile Acquisition contingent consideration (see Note C)	3,337	—	3,337
Tax benefit allocated to reduce goodwill	<u>(23)</u>	<u>—</u>	<u>(23)</u>
Balance as of March 26, 2005	479,708	12,292	492,000
Adjustment of pre-acquisition tax liability	583	—	583
Tax benefit allocated to reduce goodwill	<u>(23)</u>	<u>—</u>	<u>(23)</u>
	<u>\$480,268</u>	<u>\$12,292</u>	<u>\$ 492,560</u>

During the second quarter of 2005, the Company changed its estimate of the ultimate treatment by a tax authority of certain tax contingencies that existed as of the date of the Acquisition. This change in estimate resulted in an increase in the Company's goodwill and tax liability.

E. Warranties

The Company's wholesale segment warranty policy provides a 10-year non-prorated warranty service period on all first quality conventional bedding products. The Company's juvenile bedding products have warranty periods ranging from five years to a lifetime. The Company's policy is to accrue the estimated cost of warranty coverage at the time the sale is recorded. The following table presents a reconciliation of the Company's warranty liability for the quarters and six months ended June 25, 2005 and June 26, 2004 (in thousands):

	For the Quarters Ended		For the Six Months Ended	
	June 25, 2005	June 26, 2004	June 25, 2005	June 26, 2004
Balance at beginning of period	\$ 3,810	\$ 3,831	\$ 3,699	\$ 3,803
Additional warranties issued	1,111	1,381	2,085	2,295
Warranty settlements	(1,433)	(1,204)	(2,919)	(2,090)
Revisions of estimate	<u>692</u>	<u>138</u>	<u>1,315</u>	<u>138</u>
Balance at end of period	<u>\$ 4,180</u>	<u>\$ 4,146</u>	<u>\$ 4,180</u>	<u>\$ 4,146</u>

F. Long-Term Debt

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

	June 25, 2005	December 25, 2004
Senior credit facility:		
Revolving loan	\$ —	\$ —
Tranche C term loan	<u>391,932</u>	<u>396,600</u>
Total senior credit facility	391,932	396,600
Senior unsecured term loan	140,000	140,000
Industrial revenue bonds, 7.00%, due 2017	9,700	9,700
Industrial revenue bonds, 3.62%, due 2016	3,800	3,800
Banco Santander loan, 3.15%, due 2013	1,796	1,902
7.875% senior subordinated notes due 2014	200,000	200,000
Other, including capital lease obligations	<u>85</u>	<u>137</u>
	747,313	752,139
Less current portion	<u>(839)</u>	<u>(4,124)</u>
	<u>\$746,474</u>	<u>\$ 748,015</u>

As of June 25, 2005, the Company had availability to borrow \$64.9 million under the revolving loan after giving effect to \$10.1 million that was reserved for the Company's reimbursement obligations with respect to outstanding letters of credit. The remaining availability under the revolving loan may be utilized to meet the Company's current working capital requirements, including issuance of stand-by and trade letters of credit. The Company

also may utilize the remaining availability under the revolving loan to fund distributions, acquisitions and capital expenditures.

Depending on the Company's leverage ratio, the Company may be required to prepay the tranche C term loan with up to 50% of the Company's excess cash flow (as defined in the senior credit facility) from each fiscal year. As a result of the Company's fiscal year 2004 excess cash flow, the Company made a \$3.7 million mandatory prepayment on the tranche C term loan in March 2005. The Company prepaid \$1.0 million of the tranche C term loan in the second quarter of 2005. The next quarterly principal payment required on the tranche C term loan will be in June 2006.

The senior credit facility and the senior unsecured term loan bear interest at the Company's choice of the Eurodollar Rate or Base Rate (both as defined), plus the applicable interest rate margins as follows:

	Eurodollar Rate	Base Rate
Revolving loan	2.50%	1.50%
Tranche C term loan	2.50%	1.50%
Senior unsecured term loan	3.75%	2.75%

The weighted average interest rates per annum in effect as of June 25, 2005 for the tranche C term loan and senior unsecured term loan were 5.84% and 7.00%, respectively.

The Company has developed and implemented a policy to utilize extended Eurodollar contracts to minimize the impact of near term Eurodollar rate increases. For approximately \$325 million of the tranche C term loan and \$140 million of the senior unsecured term loan, the Company set the interest rate at the twelve month Eurodollar Rate on January 26, 2005, which fixed the Eurodollar Rate at 3.25% through January 26, 2006. To further address interest rate risk, the Company has an interest rate cap agreement for a notional amount of \$170 million which capped the Eurodollar Rate at 5.0% for the period of January 26, 2005 through January 26, 2006. The interest rate cap agreement has not been designated for hedge accounting and, accordingly, any changes in the fair value are recorded in interest expense. The fair value of the interest rate cap agreement is less than \$0.3 million. The execution of these debt instruments resulted in the Company fixing or capping the interest rate on approximately 87% of its floating rate debt as of June 25, 2005.

The 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 all the Company's active domestic subsidiaries. All the subsidiary guarantors are 100% owned by the Company. The following supplemental consolidating condensed financial statements provide additional guarantor/non-guarantor information.

Supplemental Consolidating Condensed Statements of Operations
For the Quarter Ended June 25, 2005

(In thousands)

	<u>Issuer and Guarantors</u>			<u>Eliminations</u>	<u>Consolidated</u>
	<u>Simmons Bedding Company</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Guarantor Subsidiaries</u>		
Net sales	\$(17,784)	\$ 222,739	\$ 3,087	\$ —	\$ 208,042
Cost of products sold	<u>305</u>	<u>114,771</u>	<u>2,180</u>	<u>—</u>	<u>117,256</u>
Gross profit	<u>(18,089)</u>	<u>107,968</u>	<u>907</u>	<u>—</u>	<u>90,786</u>
Operating expenses:					
Selling, general and administrative expenses	48,869	23,540	647	—	73,056
Plant closure charges	—	40	—	—	40
Amortization of intangibles	807	610	—	—	1,417
Intercompany fees	(71,072)	70,817	255	—	—
Transaction expenses	171	6	—	—	177
Licensing fees	<u>(265)</u>	<u>(2,400)</u>	<u>(150)</u>	<u>—</u>	<u>(2,815)</u>
	<u>(21,490)</u>	<u>92,613</u>	<u>752</u>	<u>—</u>	<u>71,875</u>
Operating income	3,401	15,355	155	—	18,911
Interest expense, net	12,975	199	29	—	13,203
Income from subsidiaries	<u>14,173</u>	<u>—</u>	<u>—</u>	<u>(14,173)</u>	<u>—</u>
Income before income taxes	4,599	15,156	126	(14,173)	5,708
Income tax expense (benefit)	<u>920</u>	<u>1,266</u>	<u>(157)</u>	<u>—</u>	<u>2,029</u>
Net income	<u>\$ 3,679</u>	<u>\$ 13,890</u>	<u>\$ 283</u>	<u>\$ (14,173)</u>	<u>\$ 3,679</u>

Supplemental Consolidating Condensed Statements of Operations
For the Quarter Ended June 26, 2004

(In thousands)

	<u>Issuer and Guarantors</u>			<u>Eliminations</u>	<u>Consolidated</u>
	<u>Simmons Bedding Company</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Guarantor Subsidiaries</u>		
Net sales	\$(19,064)	\$ 217,898	\$ 2,961	\$ —	\$ 201,795
Cost of products sold	<u>281</u>	<u>107,882</u>	<u>2,082</u>	<u>—</u>	<u>110,245</u>
Gross margin	(19,345)	110,016	879	—	91,550
Operating expenses:					
Selling, general and administrative expenses	45,223	27,902	480	—	73,605
Amortization of intangibles	(2,007)	810	—	—	(1,197)
Plant closure charges	—	764	—	—	764
Transaction expenses	162	500	—	—	662
Intercompany fees	(52,956)	52,708	248	—	—
Licensing fees	<u>(174)</u>	<u>(2,161)</u>	<u>(146)</u>	<u>—</u>	<u>(2,481)</u>
	<u>(9,752)</u>	<u>80,523</u>	<u>582</u>	<u>—</u>	<u>71,353</u>
Operating income (loss)	(9,593)	29,493	297	—	20,197
Interest expense, net	10,676	201	11	—	10,888
Income from subsidiaries	<u>18,715</u>	<u>—</u>	<u>—</u>	<u>(18,715)</u>	<u>—</u>
Income (loss) before income taxes	(1,554)	29,292	286	(18,715)	9,309
Income tax expense (benefit)	<u>(7,512)</u>	<u>10,792</u>	<u>71</u>	<u>—</u>	<u>3,351</u>
Net income	<u>\$ 5,958</u>	<u>\$ 18,500</u>	<u>\$ 215</u>	<u>\$ (18,715)</u>	<u>\$ 5,958</u>

Supplemental Consolidating Condensed Statements of Operations
For the Six Months Ended June 25, 2005

(In thousands)

	Issuer and Guarantors			Eliminations	Consolidated
	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 margin	(34,410)	215,216	1,396	—	182,202
Operating expenses:					
Selling, general and administrative expenses	100,349	50,650	1,127	—	152,126
Plant closure charges	—	40	—	—	40
Amortization of intangibles	1,615	1,243	—	—	2,858
Intercompany fees	(142,807)	142,348	459	—	—
Transaction expenses	171	6	—	—	177
Licensing fees	(529)	(4,009)	(328)	—	(4,866)
	(41,201)	190,278	1,258	—	150,335
Operating income	6,791	24,938	138	—	31,867
Interest expense, net	24,940	400	52	—	25,392
Income from subsidiaries	23,711	—	—	(23,711)	—
Income before income taxes	5,562	24,538	86	(23,711)	6,475
Income tax expense (benefit)	1,400	1,039	(126)	—	2,313
Net income	\$ 4,162	\$ 23,499	\$ 212	\$ (23,711)	\$ 4,162

Supplemental Consolidating Condensed Statements of Operations
For the Six Months Ended June 26, 2004

(In thousands)

	<u>Issuer and Guarantors</u>			<u>Eliminations</u>	<u>Consolidated</u>
	<u>Simmons Bedding Company</u>	<u>Guarantor Subsidiaries</u>	<u>Non- Guarantor Subsidiaries</u>		
Net sales	\$ (31,230)	\$ 450,959	\$ 5,386	\$ —	\$ 425,115
Cost of products sold	<u>594</u>	<u>225,581</u>	<u>3,935</u>	<u>—</u>	<u>230,110</u>
Gross margin	<u>(31,824)</u>	<u>225,378</u>	<u>1,451</u>	<u>—</u>	<u>195,005</u>
Operating expenses:					
Selling, general and administrative expenses	101,239	56,598	1,029	—	158,866
Amortization of intangibles	661	1,628	—	—	2,289
Plant closure charges	—	764	—	—	764
Transaction expenses	162	500	—	—	662
Intercompany fees	(106,880)	106,417	463	—	—
Licensing fees	<u>(520)</u>	<u>(4,259)</u>	<u>(283)</u>	<u>—</u>	<u>(5,062)</u>
	<u>(5,338)</u>	<u>161,648</u>	<u>1,209</u>	<u>—</u>	<u>157,519</u>
Operating income (loss)	(26,486)	63,730	242	—	37,486
Interest expense, net	21,563	397	21	—	21,981
Income from subsidiaries	<u>39,406</u>	<u>—</u>	<u>—</u>	<u>(39,406)</u>	<u>—</u>
Income (loss) before income taxes	(8,643)	63,333	221	(39,406)	15,505
Income tax expense (benefit)	<u>(18,566)</u>	<u>24,070</u>	<u>78</u>	<u>—</u>	<u>5,582</u>
Net income	<u>\$ 9,923</u>	<u>\$ 39,263</u>	<u>\$ 143</u>	<u>\$ (39,406)</u>	<u>\$ 9,923</u>

Supplemental Consolidating Condensed Balance Sheets

As of June 25, 2005

(In thousands)

	Issuer and Guarantors			Eliminations	Consolidated
	Simmons Bedding Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries		
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 14,793	\$ 15,204	\$ 1,371	\$ —	\$ 31,368
Accounts receivable	565	69,157	2,193	—	71,915
Inventories	—	31,600	882	—	32,482
Other	8,043	10,738	560	—	19,341
Total current assets	23,401	126,699	5,006	—	155,106
Property, plant and equipment, net	11,018	43,915	5,101	—	60,034
Goodwill and other intangibles, net	67,688	964,931	65	—	1,032,684
Other assets	19,451	18,698	652	—	38,801
Net investment in and advances to (from) affiliates	912,914	135,775	(1,771)	(1,046,918)	—
	<u>\$1,034,472</u>	<u>\$1,290,018</u>	<u>\$ 9,053</u>	<u>\$(1,046,918)</u>	<u>\$1,286,625</u>
LIABILITIES AND STOCKHOLDER'S EQUITY					
Current liabilities:					
Current maturities of long-term debt	\$ 395	\$ 226	\$ 218	\$ —	\$ 839
Accounts payable and accrued liabilities	44,729	61,643	1,412	—	107,784
Total current liabilities	45,124	61,869	1,630	—	108,623
Long-term debt	731,538	13,354	1,582	—	746,474
Deferred income taxes	(13,073)	168,551	177	—	155,655
Other non-current liabilities	6,120	4,588	402	—	11,110
Total liabilities	769,709	248,362	3,791	—	1,021,862
Stockholder's equity	264,763	1,041,656	5,262	(1,046,918)	264,763
	<u>\$1,034,472</u>	<u>\$1,290,018</u>	<u>\$ 9,053</u>	<u>\$(1,046,918)</u>	<u>\$1,286,625</u>

Supplemental Consolidating Condensed Balance Sheets
As of December 25, 2004
(In thousands)

	Issuer and Guarantors			Eliminations	Consolidated
	Simmons Bedding Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries		
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 15,923	\$ 7,333	\$ 598	\$ —	\$ 23,854
Accounts receivable	—	82,936	2,497	—	85,433
Inventories	—	32,622	678	—	33,300
Other	<u>10,426</u>	<u>11,646</u>	<u>577</u>	<u>—</u>	<u>22,649</u>
Total current assets	<u>26,349</u>	<u>134,537</u>	<u>4,350</u>	<u>—</u>	<u>165,236</u>
Property, plant and equipment, net	11,277	46,370	5,196	—	62,843
Goodwill and other intangibles, net	69,284	962,319	65	—	1,031,668
Other assets	20,165	21,015	807	—	41,987
Net investment in and advances to (from) affiliates	<u>910,120</u>	<u>131,043</u>	<u>19</u>	<u>(1,041,182)</u>	<u>—</u>
	<u>\$1,037,195</u>	<u>\$1,295,284</u>	<u>\$ 10,437</u>	<u>\$(1,041,182)</u>	<u>\$1,301,734</u>
LIABILITIES AND STOCKHOLDER'S EQUITY					
Current liabilities:					
Current maturities of long-term debt	\$ 3,655	\$ 241	\$ 229	\$ —	\$ 4,125
Accounts payable and accrued liabilities	<u>48,413</u>	<u>72,350</u>	<u>2,597</u>	<u>—</u>	<u>123,360</u>
Total current liabilities	<u>52,068</u>	<u>72,591</u>	<u>2,826</u>	<u>—</u>	<u>127,485</u>
Long-term debt	732,945	13,381	1,689	—	748,015
Deferred income taxes	(14,353)	168,663	465	—	154,775
Other non-current liabilities	<u>5,927</u>	<u>4,525</u>	<u>399</u>	<u>—</u>	<u>10,851</u>
Total liabilities	<u>776,587</u>	<u>259,160</u>	<u>5,379</u>	<u>—</u>	<u>1,041,126</u>
Stockholder's equity	<u>260,608</u>	<u>1,036,124</u>	<u>5,058</u>	<u>(1,041,182)</u>	<u>260,608</u>
	<u>\$1,037,195</u>	<u>\$1,295,284</u>	<u>\$ 10,437</u>	<u>\$(1,041,182)</u>	<u>\$1,301,734</u>

Note: The Company has revised its presentation of the previously reported supplemental consolidating condensed guarantor and non-guarantor subsidiaries' balance sheets as of December 25, 2004 to reflect the following:

- The change in classification of a \$515.0 million credit balance previously reported in the Guarantor subsidiaries' line item "net investment in and advances to (from) affiliates" and a \$515.0 million debit balance previously reported in the Guarantor subsidiaries' "stockholder's equity", to the Eliminations line items "net investment in and advances to (from) affiliates" and "stockholder's equity". The adjustment relates principally to the push down of certain purchase accounting adjustments to subsidiaries;
- The correction of intercompany balances previously netted in error against the Guarantor subsidiaries', Non-Guarantor subsidiaries', and Eliminations line item "stockholder's equity" totaling a \$491.9 million credit balance, a \$1.7 million debit balance, and a \$490.2 million debit balance, respectively. The amounts have been correctly classified in this revised presentation in the line items "net investment in and advances to (from) affiliates" and "stockholder's equity"; and
- The combining of a \$366.1 million credit balance previously reported in the Guarantor subsidiaries' line item "net due to (from) subs" and a \$366.1 million debit balance previously reported in the Eliminations line item "net due to (from) subs" into the line item "net investment in and advances to (from) affiliates".

The net effect of the above changes in classification and corrections was to increase Guarantor subsidiaries' total assets by \$640.8 million, decrease the Non-Guarantor subsidiaries' total assets by \$1.7 million and decrease the Eliminations total assets by \$639.1 million. The change in classifications, combining of balance sheet line items and corrections had no effect on the audited consolidated balance sheet as of December 25, 2004.

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

	<u>Issuer and Guarantors</u>			<u>Eliminations</u>	<u>Consolidated</u>
	<u>Simmons Bedding Company</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Guarantor Subsidiaries</u>		
Net cash provided by (used in) operating activities	\$ 4,901	\$ 14,517	\$ (870)	\$ —	\$ 18,548
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:					
Repayment of long-term obligations	(4,667)	(41)	(118)	—	(4,826)
Receipt from (distribution to) affiliates	—	(2,069)	1,790	—	(279)
Net cash provided by (used in) financing activities	(4,667)	(2,110)	1,672	—	(5,105)
Net effect of exchange rate change	—	—	(6)	—	(6)
Change in cash and cash equivalents	(1,130)	7,869	775	—	7,514
Cash and cash equivalents:					
Beginning of period	15,923	7,333	598	—	23,854
End of period	<u>\$14,793</u>	<u>\$ 15,202</u>	<u>\$ 1,373</u>	<u>\$ —</u>	<u>\$ 31,368</u>

Supplemental Consolidating Condensed Statements of Cash Flows
For the Six Months Ended June 26, 2004

(In thousands)

	<u>Issuer and Guarantors</u>			<u>Eliminations</u>	<u>Consolidated</u>
	<u>Simmons Bedding Company</u>	<u>Guarantor Subsidiaries</u>	<u>Non-Guarantor Subsidiaries</u>		
Net cash provided by (used in) operating activities	\$(32,692)	\$ 69,117	\$ 1,773	\$ —	\$ 38,198
Cash flows from investing activities:					
Purchase of property, plant and equipment, net	(2,899)	(2,852)	(977)	—	(6,728)
Proceeds from sale of Gallery Corp., net	6,495	—	—	—	6,495
Other, net	105	—	—	—	105
Net cash provided by (used in) investing activities	3,701	(2,852)	(977)	—	(128)
Cash flows from financing activities:					
Repayment of long-term obligations, net	(16,960)	(601)	(116)	—	(17,677)
Receipt from (distribution to) affiliates	66,127	(63,402)	(1,800)	—	925
Payment of financing fees	(601)	—	—	—	(601)
Net cash provided by (used in) financing activities	48,566	(64,003)	(1,916)	—	(17,353)
Net effect of exchange rate change	—	—	(10)	—	(10)
Change in cash and cash equivalents	19,575	2,262	(1,130)	—	20,707
Cash and cash equivalents:					
Beginning of period	615	667	2,388	—	3,670
End of period	\$ 20,190	\$ 2,929	\$ 1,258	\$ —	\$ 24,377

G. Segment Information

The Company's 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 bedding products to retail customers and institutional users of bedding products, such as the hospitality industry; (ii) the manufacture and distribution of branded 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 (iv) the sale to consumers of product returns, off-quality product and excess inventory through retail outlet stores.

The retail bedding segment currently operates specialty sleep stores in Oregon and Washington that sell to consumers principally premium branded bedding products. On May 1, 2004, the Company sold its retail bedding subsidiary, Mattress Gallery (see Note C to the condensed consolidated financial statements for further explanation).

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, non-cash stock compensation expenses, and other 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 June 25, 2005
(In thousands)

	Wholesale Bedding	Retail	Eliminations	Totals
Net sales to external customers	\$ 189,283	\$18,759	\$ —	\$ 208,042
Intersegment net sales	3,414	—	(3,414)	—
Adjusted EBITDA	25,848	1,537	92	27,477
Depreciation and amortization expense	6,232	427	—	6,659
Expenditures for long-lived assets	1,032	176	—	1,208
Segment assets	1,260,724	27,406	(1,505)	1,286,625
Reconciliation of EBITDA and Adjusted EBITDA to net income:				
Net income	\$ 2,943	\$ 644	\$ 92	\$ 3,679
Depreciation and amortization	6,232	427	—	6,659
Income taxes	1,661	368	—	2,029
Interest expense, net	13,200	3	—	13,203
Interest income	11	1	—	12
EBITDA	24,047	1,443	92	25,582
Reorganization costs	1,345	—	—	1,345
Management fees	239	94	—	333
Transaction expenses	177	—	—	177
Plant closing costs	40	—	—	40
Adjusted EBITDA	<u>\$ 25,848</u>	<u>\$ 1,537</u>	<u>\$ 92</u>	<u>\$ 27,477</u>

Quarter Ended June 26, 2004

(In thousands)

	Wholesale Bedding	Retail	Eliminations	Totals
Net sales to external customers	\$ 182,597	\$19,198	\$ —	\$ 201,795
Intersegment net sales	5,138	—	(5,138)	—
Adjusted EBITDA	28,092	514	301	28,907
Depreciation and amortization expense	2,996	101	—	3,097
Expenditures for long-lived assets	4,701	215	—	4,916
Segment assets	1,243,320	29,945	(2,106)	1,271,159
Reconciliation of EBITDA and Adjusted EBITDA to net income (loss):				
Net income (loss)	\$ 6,168	\$ (511)	\$ 301	\$ 5,958
Depreciation and amortization	2,996	101	—	3,097
Income taxes	3,508	(157)	—	3,351
Interest expense, net	10,840	48	—	10,888
Interest income	31	—	—	31
EBITDA	23,543	(519)	301	23,325
Plant opening, closing charges	4,722	—	—	4,722
Mattress Gallery transaction expenses	162	500	—	662
Management fees	(64)	533	—	469
Other	(271)	—	—	(271)
Adjusted EBITDA	<u>\$ 28,092</u>	<u>\$ 514</u>	<u>\$ 301</u>	<u>\$ 28,907</u>

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	43,635	3,653	170	47,458
Depreciation and amortization expense	12,370	753	—	13,123
Expenditures for long-lived assets	2,156	430	—	2,586
Segment assets	1,260,724	27,406	(1,505)	1,286,625
Reconciliation of EBITDA and Adjusted EBITDA to net income:				
Net income	\$ 2,254	\$ 1,738	\$ 170	\$ 4,162
Depreciation and amortization	12,370	753	—	13,123
Income taxes	1,348	965	—	2,313
Interest expense, net	25,386	6	—	25,392
Interest income	47	1	—	48
EBITDA	41,405	3,463	170	45,038
Reorganization costs	1,345	—	—	1,345
Management fees	563	190	—	753
Management severance	105	—	—	105
Transaction expenses	177	—	—	177
Plant closing costs	40	—	—	40
Adjusted EBITDA	<u>\$ 43,635</u>	<u>\$ 3,653</u>	<u>\$ 170</u>	<u>\$ 47,458</u>

Six Months Ended June 26, 2004

(In thousands)

	Wholesale Bedding	Retail	Eliminations	Totals
Net sales to external customers	\$ 380,810	\$44,305	\$ —	\$ 425,115
Intersegment net sales	14,027	—	(14,027)	—
Adjusted EBITDA	64,848	1,617	(261)	66,204
Depreciation and amortization expense	10,300	417	—	10,717
Expenditures for long-lived assets	6,052	676	—	6,728
Segment assets	1,243,320	29,945	(2,106)	1,271,159
Reconciliation of EBITDA and Adjusted EBITDA to net income (loss):				
Net income (loss)	\$ 14,368	\$ (4,184)	\$ (261)	\$ 9,923
Depreciation and amortization	10,300	417	—	10,717
Income taxes	5,968	(386)	—	5,582
Interest expense, net	21,883	98	—	21,981
Interest income	75	—	—	75
EBITDA	<u>52,594</u>	<u>(4,055)</u>	<u>(261)</u>	<u>48,278</u>
Non-cash stock compensation expense	3,308	—	—	3,308
Transaction related expenditures, including cost of products sold	2,640	3,844	—	6,484
Plant opening, closing charges	6,951	—	—	6,951
Mattress Gallery transaction expenses	162	500	—	662
Management fees	(490)	1,328	—	838
Other expenses	(317)	—	—	(317)
Adjusted EBITDA	<u>\$ 64,848</u>	<u>\$ 1,617</u>	<u>\$ (261)</u>	<u>\$ 66,204</u>

H. People Realignment Plan

In connection with a Company cost savings initiative, a people realignment plan for the Company's salaried associates was implemented in the second and third quarters of 2005. The people realignment plan consisted of three phases. In the first phase, a voluntary early retirement program was offered to eligible salaried associates. Those associates participating in the early retirement program were offered benefits including severance payments and continued health insurance. The Company recorded the costs of the early retirement program when associates accepted the offer, which was during the second quarter of 2005. The cost of this early retirement program was \$0.7 million and is reflected in selling, general and administrative expense in the accompanying condensed consolidated statement of operations.

The second and third phases of the people realignment plan included voluntary and involuntary permanent reductions of the Company's salaried associates. Associates terminated under these two phases were offered certain benefits which included severance payments,

outplacement services and health insurance. The Company recorded the costs of the voluntary permanent terminations once the associate offered their resignation and the Company accepted, which was in the third quarter of 2005. The Company recorded the costs of the involuntary permanent terminations once the Company determined the final number of employees to be involuntarily separated and the plan was communicated to the associates, which was in the third quarter of 2005. The costs of the second and third phases of the people realignment plan are currently estimated to be \$1.7 million in the aggregate and will be recorded in the Company's third quarter 2005 condensed consolidated statement of operations.

The Company anticipates the people realignment plan will result in annualized compensation, fringe and benefit savings of approximately \$5.0 million.

I. Plant Closing and Opening Charges

The Company's Columbus, Ohio manufacturing facility was closed in April 2004. The Company incurred plant closure charges of approximately \$0.8 million of severance, retention, rent, and transfer of equipment costs during the second quarter of fiscal year 2004 related to this closing. The Company wrote off inventory and incurred other miscellaneous charges of \$0.2 million as a result of the closure of the plant, which was included in cost of goods sold during the second quarter of 2004. Additionally, the Company dismantled and abandoned equipment resulting in a \$0.2 million charge to selling, general and administrative expenses during the second quarter of 2004.

The Company opened a new manufacturing facility in Hazleton, Pennsylvania on March 15, 2004. The Company incurred non-recurring start-up costs, net of local and state training grants, related to the openings of approximately \$3.0 million and \$5.8 million for the quarter and six months ended June 26, 2004. The start-up costs include travel and relocation, rent, utilities, repair and maintenance, and training expenses totaling \$1.5 million and \$3.2 million for the quarter and six months ended June 26, 2004, which are included in cost of products sold, and incremental distribution costs of \$1.5 million and \$2.6 million for the quarter and six months ended June 26, 2004, which are included in selling, general and administrative expenses. The incremental distribution expense resulted from the extra miles driven to service the customers that were previously serviced by the Company's closed manufacturing facilities.

In May 2005 and at the end of the lease term, the Company moved its juvenile manufacturing facility formerly located in Oshkosh, Wisconsin to a temporary manufacturing facility. The Company anticipates moving to a permanent facility in Neenah, Wisconsin during the third quarter of 2005.

J. 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.

K. Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123 (Revised 2004), *Share-Based Payment – An Amendment of FAS 123 and FAS 95*, (“SFAS 123R”). SFAS 123R requires that compensation cost relating to share-based payment transactions be recognized in financial statements based upon the fair value of the award. SFAS 123R eliminates the option to account for the cost of stock-based compensation using the intrinsic value method as allowed under APB Opinion No. 25, *Accounting for Stock Issued to Employees*. The Company is considered a non-public entity as defined by SFAS 123R. SFAS 123R is effective for non-public entities for fiscal years beginning after December 15, 2005. The Company expects to adopt SFAS 123R as of the beginning of its fiscal year 2006. The Company does not anticipate that SFAS 123R will have a material effect on its consolidated financial statements.

In December 2004, the Financial Accounting Standards Board issued SFAS No. 153, *Exchanges of Nonmonetary Assets – An Amendment of APB Opinion No. 29*, (“SFAS 153”). SFAS 153, in contrast to APB No. 29, requires exchanges of nonmonetary assets to be accounted for based on the fair market value of the assets exchanged, rather than at their historical cost. The provisions of SFAS 153 are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005 and companies must apply the standard prospectively. The Company expects to adopt SFAS 153 as of the beginning of fiscal year 2006 and does not anticipate that SFAS 153 will have a material effect on its consolidated financial statements.

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 25, 2004, including related notes, and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our 2004 Annual Report on Form 10-K, and the unaudited interim financial statements included elsewhere in this report.

Recent Events

People Realignment Plan

In connection with our cost savings initiative, a people realignment plan for our salaried associates was implemented in the second and third quarters of 2005. The people realignment plan consisted of three phases. In the first phase, a voluntary early retirement program was offered to eligible salaried associates. Those associates participating in the early retirement program were offered benefits including severance payments and continued health insurance. We recorded the costs of the early retirement program when associates accepted the offer, which was during the second quarter of 2005. The cost of this early retirement program was \$0.7 million and is reflected in selling, general and administrative expense in the accompanying condensed consolidated statement of operations.

The second and third phases of the people realignment plan included voluntary and involuntary permanent reductions of our salaried associates. Associates terminated under these two phases were offered certain benefits which included severance payments, outplacement services and health insurance. We recorded the costs of the voluntary permanent terminations once the associate offered their resignation and we accepted, which was in the third quarter of 2005. We recorded the costs of the involuntary permanent terminations once we determined the final number of employees to be involuntarily separated and the plan was communicated to the associates, which was in the third quarter of 2005. The costs of the second and third phases of the people realignment plan are currently estimated to be \$1.7 million in the aggregate and will be recorded in our third quarter 2005 condensed consolidated statement of operations.

We anticipate the people realignment plan will result in annualized compensation, fringe and benefit savings of approximately \$5.0 million.

Restructuring of our Corporate Management Team

In connection with the people realignment plan, we restructured our corporate management team. As a result of the restructuring, our then President, Robert W. Hellyer, left the Company to pursue other professional opportunities and our Chairmen and CEO, Charles R. Eitel, assumed certain of Mr. Hellyer's responsibilities.

Additionally, we appointed Timothy F. Oakhill as our Senior Vice President of Marketing and Licensing. Mr. Oakhill, who has been with the Company for eight years, was instrumental in growing the BackCare® and BackCare Kids® brands. Most recently, Mr. Oakhill was Vice President of International and Domestic Licensing.

On July 30, 2005, we hired Robert P. Burch as our Executive Vice President – Operations. Mr. Burch comes to Simmons after 26 years with office furniture manufacturer, Steelcase, Inc., where Mr. Burch most recently held the position of Vice President of Order Fulfillment for North America.

On August 9, 2005, we named Stephen G. Fendrich as our Executive Vice President – Sales. Mr. Fendrich has been Chief Executive Officer and President of our SC Holdings, Inc. and Sleep Country USA, Inc. subsidiaries since September 2002. Mr. Fendrich will continue in his Sleep Country role until a successor is named. Kevin Damewood, previously Senior Vice President – Sales, will assume the duties of Divisional Vice President – Sales for the Northeast Region.

Labor Unions

Both the Steelworkers and Teamsters labor unions at our Los Angeles manufacturing facility ratified 4-year collective bargaining agreements in July 2005. These agreements are effective starting in October 2005 through September 2009. We do not expect either contract to have a significant impact on our future operating results.

Results of Operations

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

	Quarters Ended		Six Months Ended	
	June 25, 2005	June 26, 2004	June 25, 2005	June 26, 2004
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of products sold	56.4%	54.6%	55.9%	54.1%
Gross margin	43.6%	45.4%	44.1%	45.9%
Operating expenses:				
Selling, general and administrative expenses	35.1%	36.5%	36.8%	37.4%
Plant closure charges	0.0%	0.4%	0.0%	0.2%
Amortization of intangibles	0.7%	-0.6%	0.7%	0.5%
Transaction expenses	0.1%	0.3%	0.0%	0.2%
Licensing fees	-1.4%	-1.2%	-1.2%	-1.2%
	<u>34.5%</u>	<u>35.4%</u>	<u>36.3%</u>	<u>37.1%</u>
Operating income	9.1%	10.0%	7.7%	8.8%
Interest expense, net	6.3%	5.4%	6.1%	5.2%
Income before income taxes	2.7%	4.6%	1.6%	3.6%
Income tax expense	1.0%	1.7%	0.6%	1.3%
Net income	<u>1.8%</u>	<u>3.0%</u>	<u>1.0%</u>	<u>2.3%</u>

Quarter Ended June 25, 2005 as Compared to Quarter Ended June 26, 2004

Net sales. The following table presents our net sales and the dollar and percentage change by segment for the quarter ended June 25, 2005 compared to the quarter ended June 26, 2004:

	2005	2004	\$ increase (decrease)	% increase (decrease)
			(in millions)	
Wholesale bedding segment	\$ 192.7	\$ 187.7	\$ 5.0	2.6%
Retail bedding segment	18.8	19.2	(0.4)	-2.3%
Eliminations	(3.5)	(5.1)	1.6	-31.4%
Consolidated net sales	<u>\$ 208.0</u>	<u>\$ 201.8</u>	<u>\$ 6.2</u>	<u>3.1%</u>

Wholesale bedding segment net sales increased \$5.0 million, or 2.6%, due primarily to the addition of \$6.2 million of net sales of juvenile products as a result of the acquisition of the crib mattress and related soft goods of Simmons Juvenile Products Company, Inc. in

August 2004 (the “Juvenile Acquisition”). Our conventional bedding net sales declined \$0.9 million, or 0.5%, principally due to our unit volume declining 7.4%, or an estimated \$16.1 million, for the quarter ended June 25, 2005 compared to the quarter ended June 26, 2004. Partially offsetting our decline in conventional bedding unit volume, our conventional bedding average unit selling price (“AUSP”) increased 6.0%, or an estimated \$12.4 million, for the quarter ended June 25, 2005 compared to the quarter ended June 26, 2004. Our improvement in conventional bedding AUSP was primarily attributable to the shipment of our new product lines in 2005 which, on average, sell at higher prices than our 2004 product lines.

The second quarter conventional bedding unit decline of 7.4% was an improvement compared to the 15.2% unit decline in the first quarter of 2005 versus the comparable period of 2004. The second quarter unit decline was due principally to less units sold at “velocity” retail price points below \$500 and premium retail price points above \$2,000. To address these volume declines, we have introduced a new Deep Sleep® product line at the recently completed Las Vegas Furniture Market that better targets velocity retail price points which will be rolled-out between August 2005 and January 2006. Additionally, during the second quarter, we introduced new innerspring premium priced products to complement our HealthSmart™ products, and the Beautyrest® Caresse® visco elastic (“memory foam”) products. Our increase in the second quarter unit sales versus the first quarter 2005 was a result of these new products introduced during the second quarter, as well as other pricing and product modifications which were made commencing in March 2005.

For the quarters ended June 25, 2005 and June 26, 2004, our wholesale bedding segment net sales reflect a reduction of \$17.7 million and \$19.5 million, respectively, for cash consideration paid to our customers for certain promotional programs, allowances and volume rebates. Our sales reductions decreased principally due to more of our co-op advertising costs meeting the criteria of a selling expense versus a sales reduction. For the quarter ended June 25, 2005, as a percentage of our sales, our aggregate co-op advertising expenditures, regardless of whether reported as a selling expense or a sales reduction were 0.3 percentage points lower than the aggregate co-op advertising expenditures for the quarter ended June 26, 2004.

Retail bedding segment sales in the second quarter 2005 decreased \$0.4 million, or 2.3%, compared to the second quarter 2004 as a result of the sale of our Mattress Gallery retail operations on May 1, 2004. Mattress Gallery contributed \$3.0 million of retail sales for the quarter ended June 26, 2004. On a comparable store basis, sales for our retail stores increased 14.6% for the quarter ended June 25, 2005 versus the quarter ended June 26, 2004. Retail segment same store sales have benefited from increased advertising by our retail segment and an improved retail sales environment in Washington and Oregon.

Gross Margin. The following table presents our gross profit by segment, gross margin as a percentage of segment net sales, and the gross margin percentage point change by segment for the quarter ended June 25, 2005 compared to the quarter ended June 26, 2004:

	Gross Profit		Gross Margin		Margin % Point Change
	2005	2004	2005	2004	
	(in millions)				
Wholesale bedding segment	\$ 80.7	\$ 81.6	41.9%	43.4%	-1.5%
Retail bedding segment	10.0	9.7	53.1%	50.4%	2.7%
Eliminations	0.1	0.3	-2.8%	-5.9%	3.1%
Consolidated	<u>\$ 90.8</u>	<u>\$ 91.6</u>	43.6%	45.4%	-1.8%

Our wholesale bedding segment gross margin declined 1.5 percentage points due primarily to (i) an increase in our conventional bedding material costs of 1.5 percentage points due principally to the inflation of raw material costs and the added material costs to make our products sold in the State of California meet California's new open flame resistance standards which became effective January 1, 2005 and (ii) the selling in 2005 of juvenile products, which sell at lower margins, as a result of the Juvenile Acquisition, which resulted in a 0.6 percentage point decline in gross margin. Partially offsetting the decrease in our wholesale bedding segment gross margin, our conventional bedding labor and overhead costs in the aggregate decreased 0.6 percentage points primarily due to charges incurred in the second quarter of 2004 of \$1.7 million, or 0.9 percentage points, related to the opening of Hazleton, Pennsylvania manufacturing facility and the closure of our Columbus, Ohio manufacturing facility.

Our retail bedding segment gross margin improved 2.7 percentage points principally due to (i) the sale of our Mattress Gallery retail operations in May 2004, which had a lower margin product sales mix than our Sleep Country retail operations; and (ii) the gross margins at our Sleep Country retail operations improving due to a shift in sales mix to products that have higher gross margins.

Selling, general and administrative expenses ("SG&A"). The following table presents our SG&A dollar amount by segment, as a percentage of segment net sales and the percentage point change by segment for the quarter ended June 25, 2005 compared to the quarter ended June 26, 2004:

	SG&A		As a % of Segment Net Sales		Margin % Point Change
	2005	2004	2005	2004	
	(in millions)				
Wholesale bedding segment	\$ 64.2	\$ 63.8	33.3%	34.0%	-0.7%
Retail bedding segment	8.9	9.8	47.2%	50.8%	-3.6%
Consolidated	<u>\$ 73.1</u>	<u>\$ 73.6</u>	35.1%	36.5%	-1.3%

Our wholesale bedding segment SG&A for the second quarter of 2004 included \$1.5 million, or 0.8 percentage points, of non-recurring distribution expense related to the incremental miles driven to service customers from existing manufacturing facilities while we were opening and closing manufacturing facilities during 2004. Exclusive of the impact of the incremental distribution expense on our SG&A for the second quarter of 2004, our 2005 wholesale bedding segment SG&A increased 0.1 percentage points principally due to higher (i) distribution expense of \$2.0 million, or 0.9 percentage points, due principally to higher fuel costs and more miles driven; (ii) national advertising expenditures of \$1.5 million, or 0.7 percentage points, due to the completion of advertising commitments related to our HealthSmart™ national advertising campaign that was curtailed at the end of the first quarter of 2005; (iii) co-op advertising expenses of \$2.0 million, or 0.9 percentage points, due to more of our expenditures meeting the criteria of a selling expense versus a sales reduction; (iv) consulting fees of \$1.0 million, or 0.5 percentage points, due to our use of outside consultants in connection with our cost savings initiative and Sarbanes-Oxley compliance efforts; and (v) severance expense of \$0.7 million, or 0.3 percentage points, due to the voluntary early retirement phase of our people realignment plan.

Partially offsetting these increases, our wholesale bedding segment SG&A benefited from lower (i) provisions for bad debts of \$2.3 million, or 1.3 percentage points, as a result of our improved customer credit profile and receivables aging, combined with the favorable settlement of a customer bankruptcy claim; (ii) bonus expense of \$1.2 million, or 0.7 percentage points, due to lower anticipated management bonus payouts for 2005 than in 2004; and (iii) selling expenses of \$0.9 million, or 0.7 percentage points, due to our lower sales volume.

Our retail segment SG&A decreased 3.6 percentage points primarily due to the sale of our Mattress Gallery retail operations as discussed above and our Sleep Country retail operations growing their same store sales which allows Sleep Country to better leverage their fixed costs, such as salaries, advertising and rent.

Plant Closure Charges. For the quarter ended June 25, 2005, we incurred less than \$0.1 million of plant closure charges related to the closing of our juvenile manufacturing facility located in Oshkosh, Wisconsin and the relocation to a temporary manufacturing facility. We anticipate moving from the temporary manufacturing facility into a permanent facility in Neenah, Wisconsin during the third quarter of 2005. For the quarter ended June 26, 2004, we incurred \$0.8 million of plant closure charges related to the closing of our Columbus, Ohio manufacturing facility in April. The plant closure charges consisted of severance, retention, rent and costs to transfer equipment.

Amortization of Intangibles. For the quarter ended June 25, 2005, amortization of intangibles increased \$2.6 million to \$1.4 million from \$(1.2) million for the quarter ended June 26, 2004. The increase in amortization expense is attributable to the purchase price allocation associated with the Acquisition which was not finalized until the second quarter of 2004. Prior to the finalization of the purchase price allocation, the amortization of intangibles was recorded based upon a preliminary valuation of the intangible assets.

Transaction Expenses. For the quarter ended June 25, 2005, we incurred \$0.2 million in costs related to an acquisition that was not consummated. For the quarter ended June 26, 2004, we incurred transaction expenses of \$0.7 million related to the sale of Mattress Gallery in May 2004.

Licensing Fees. For the quarter ended June 25, 2005, licensing fees increased \$0.3 million, or 13.5%, to \$2.8 million from \$2.5 million for the quarter ended June 26, 2004. Licensing fees increased primarily due to improved sales for certain of our domestic licensees during the second quarter 2005 and additional royalties identified through a sales audit of a domestic licensee.

Interest Expense, Net. For the quarter ended June 25, 2005, interest expense increased \$2.3 million, or 21.3%, to \$13.2 million from \$10.9 million for the quarter ended June 26, 2004. Interest expense increased due to higher LIBOR base rates on our senior credit facility, partially offset by lower average outstanding borrowings for the quarter ended June 25, 2005 compared to the quarter ended June 26, 2004.

Income Taxes. The combined estimated federal, state, and foreign effective income tax rate of 35.5% for the quarter ended June 25, 2005 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. The combined estimated federal, state, and foreign effective income tax rate of 36.0% for the quarter ended June 26, 2004 differed from the federal statutory rate of 35.0% primarily due to (i) state tax rate benefits realized as a result of a decrease in the rate at which our U.S. deferred tax assets and liabilities were recorded; (ii) the tax effect of a valuation allowance increase for Sleep Country's net deferred tax assets; and (iii) state income tax expense.

Six Months Ended June 25, 2005 as Compared to Six Months Ended June 26, 2004

Net sales. The following table presents our net sales and the dollar and percentage change by segment for the six months ended June 25, 2005 compared to the six months ended June 26, 2004:

	2005	2004 (in millions)	\$ increase (decrease)	% increase (decrease)
Wholesale bedding segment	\$ 382.3	\$ 394.8	\$ (12.5)	-3.2%
Retail bedding segment	37.9	44.3	(6.4)	-14.5%
Eliminations	(6.6)	(14.0)	7.4	-53.2%
Consolidated net sales	<u>\$ 413.6</u>	<u>\$ 425.1</u>	<u>\$ (11.5)</u>	<u>-2.7%</u>

Wholesale bedding segment net sales decreased \$12.5 million, or 3.2%, due principally to a decline in conventional bedding net sales of \$23.5 million, or 6.0%, partially offset by an additional \$11.9 million of net sales resulting from sales of juvenile products. Our decrease in conventional bedding net sales was principally due to a decline in our conventional bedding unit volume of 11.4%, or an estimated \$51.4 million in sales, for the six months ended June 25, 2005 compared to the six months ended June 26, 2004. Partially offsetting our decline in conventional bedding unit volume, our AUSP increased 6.3%, or an estimated \$23.9 million in sales, for the six months ended June 25, 2005 compared to the six months ended June 26, 2004. Our improvement in conventional bedding AUSP was primarily attributable to the shipment of our new product lines in 2005 which, on average, sell for higher prices than our 2004 product lines.

The first six months 2005 unit decline was due principally to (i) less units sold at "velocity" retail price points below \$500; (ii) for the first quarter of 2005 all of our premium priced products included the HealthSmart™ feature, which was not as successful as our previous premium priced products; and (iii) the rollout of our 2005 product lines which were initially not competitively priced at certain retail price points between \$500 to \$1,000. During the second quarter 2005, we introduced new innerspring premium priced products to complement our HealthSmart™ products, and the Beautyrest® Caresse® visco elastic ("memory foam") products. As a result of these new product introductions, as well as other pricing and product modifications made commencing in March 2005, our second quarter unit sales increased versus the first quarter of 2005. To further address the volume declines at velocity retail price points, we introduced a new Deep Sleep® product line at the recently completed Las Vegas Furniture Market that better targets velocity retail price points. This new product line will be rolled-out between August 2005 and January 2006.

For the six months ended June 25, 2005 and June 26, 2004, our wholesale bedding segment net sales reflect a reduction of \$34.7 million and \$32.1 million, respectively, for cash consideration paid to our customers for certain promotional programs, allowances and volume rebates. Our sales reductions increased principally due to more of our co-op advertising spending meeting the criteria of a sales reduction versus a selling expense. As a percentage of our sales, our aggregate co-op advertising expenditures, regardless of whether reported as a selling expense or a sales reduction, for the six months ended June 25, 2005, were comparable with the aggregate co-op advertising expenditures for the six months ended June 26, 2004.

Retail bedding segment sales decreased as a result of the sale of our Mattress Gallery retail operations on May 1, 2004. Mattress Gallery contributed \$12.9 million of retail sales for the six months ended June 26, 2004. On a comparable store basis, sales for our retail stores increased 18.4% for the six months ended June 25, 2005 versus the six months ended June 26, 2004. Retail segment same store sales have benefited from increased advertising and an improved retail sales environment in Washington and Oregon.

Gross Margin. The following table presents our gross profit, gross margin as a percentage of segment net sales, and the gross margin percentage point change by segment for the six months ended June 25, 2005 compared to the six months ended June 26, 2004.

	Gross Profit		Gross Margin		Margin % Point Change
	2005	2004	2005	2004	
	(in millions)				
Wholesale bedding segment	\$ 161.7	\$ 176.8	42.3%	44.8%	-2.5%
Retail bedding segment	20.2	18.4	53.4%	41.6%	11.8%
Eliminations	0.3	(0.2)	-3.7%	1.9%	-5.6%
Consolidated	<u>\$ 182.2</u>	<u>\$ 195.0</u>	44.1%	45.9%	-1.8%

For the six months ended June 26, 2004, our wholesale bedding segment gross margin was negatively impacted by (i) \$2.6 million, or 0.7 percentage points, as a result of the selling of inventory recorded at fair market value in connection with the purchase accounting associated with the December 19, 2003 acquisition of the company by affiliates of Thomas H. Lee Equity Fund V (the "Acquisition"); and (ii) \$3.4 million, or 0.9 percentage points, as a result of charges related to the opening of our Hazleton, Pennsylvania manufacturing facility in March 2004 and the closure of our Jacksonville, Florida and Columbus, Ohio manufacturing facilities in December 2003 and April 2004, respectively. Exclusive of the effects of the selling of the marked-up inventory and the plant opening and closing charges in the six months ended June 26, 2004, our wholesale bedding segment gross margin declined 4.1 percentage points in the first six months of 2005. Our decline in gross margin was due primarily to (i) an increase in our conventional bedding material costs of 2.2 percentage points due principally to the inflation of raw material costs and the added material costs to make our products sold in the State of California meet California's new open flame resistance standards that became effective January 1, 2005; (ii) an increase in overhead costs of 1.3 percentage points due principally to the decline in our unit volume as discussed above and operating inefficiencies resulting from the ramp-up of production at our manufacturing facilities in Waycross, Georgia and Hazleton, Pennsylvania, which opened in March 2004 and August 2004, respectively; and (iii) the selling of juvenile products, which sell at lower margins, in 2005 as a result of the Juvenile Acquisition, which resulted in a 0.5 percentage point decline in gross margin.

Our retail bedding segment gross margin improved 11.8 percentage points principally due to the selling of inventory in 2004 recorded at fair market value in connection with Acquisition. Exclusive of the effects of the selling of the marked-up inventory in the six months ended June 26, 2004, our retail bedding segment gross margin improved 3.1 percentage points. Our retail bedding segment gross margin benefited from (i) the sale of our Mattress Gallery retail operations in May 2004, which had a lower margin product sales mix than our Sleep Country retail operations; and (ii) our Sleep Country retail operations shift in sales mix to products that have higher gross margins.

Selling, general and administrative expenses (“SG&A”). The following table presents our SG&A dollar amount by segment, as a percentage of segment net sales and the percentage point change by segment for the six months ended June 25, 2005 compared to the six months ended June 26, 2004:

	SG&A		As a % of Segment Net Sales		Margin % Point Change
	2005	2004	2005	2004	
	(in millions)				
Wholesale bedding segment	\$ 134.8	\$ 136.1	35.3%	34.5%	0.8%
Retail bedding segment	17.3	22.8	45.8%	51.5%	-5.7%
Consolidated	<u>\$ 152.1</u>	<u>\$ 158.9</u>	36.8%	37.4%	-0.6%

Our wholesale bedding segment SG&A for the first six months 2004 included \$2.6 million, or 0.7 percentage points, of non-recurring distribution expense related to the incremental miles driven to service customers from existing manufacturing facilities while we were opening and closing manufacturing facilities during 2004. Exclusive of the impact of the incremental distribution expense on our SG&A for the first six months of 2004, our 2005 wholesale bedding segment SG&A increased 1.5 percentage points principally due to higher (i) national advertising of \$6.1 million, or 1.6 percentage points, due to our HealthSmart™ national advertising campaign that was curtailed at the end of the first quarter of 2005; (ii) distribution costs of \$3.0 million, or 0.9 percentage points, resulting from higher fuel costs and more miles driven to service our customers; (iii) corporate function expenses of \$2.2 million, or 0.6 percentage points, due to our biannual national leadership meeting which occurred in January 2005; (iv) consulting fees of \$1.3 million, or 0.4 percentage points, due to our use of outside consultants in connection with our cost savings initiative and Sarbanes-Oxley compliance efforts; and (v) severance expense of \$0.7 million, or 0.2 percentage points, due to the voluntary early retirement phase of our people realignment plan.

Partially offsetting these increases, our wholesale bedding segment SG&A benefited from lower (i) non-cash stock compensation expense of \$3.3 million, or 0.8 percentage points, as a result of the change in the fair market value of the equity held in our indirect parent’s, Simmons Company, deferred compensation plan that was terminated in June 2004; (ii) provision for bad debts of \$2.3 million, or 0.6 percentage points, as a result of improved customer credit profile and receivables aging, combined with the favorable settlement of a customer bankruptcy claim; (iii) selling expenses of \$3.0 million, or 0.5 percentage points, due principally to our lower sales volume; (iv) bonus expense of \$2.9 million, or 0.7 percentage points, due to a lower anticipated management bonus payout for 2005 than in 2004.

Our retail segment SG&A decreased 5.7 percentage points primarily due to the sale of our Mattress Gallery retail operations as discussed above and our Sleep Country retail operations growing their same store sales which allows Sleep Country to better leverage their fixed costs, such as salaries, advertising and rent.

Plant Closure Charges. For the six months ended June 25, 2005, we incurred less than \$0.1 million of plant closure charges related to the closing of our juvenile manufacturing facility located in Oshkosh, Wisconsin and the relocation to a temporary manufacturing facility. The Company anticipates moving into a permanent facility in Neenah, Wisconsin during the third quarter of 2005. For the six months ended June 26, 2004, we incurred \$0.8 million of plant closure charges related to the closing of our Columbus, Ohio manufacturing facility in April. The plant closure charges consisted of severance, retention, rent and costs to transfer equipment.

Amortization of Intangibles. For the six months ended June 25, 2005, amortization of intangibles increased \$0.6 million, or 24.9%, to \$2.9 million from \$2.3 million for the six months ended June 26, 2004. The increase is attributable to the amortization of the customer contracts obtained in the Juvenile Acquisition.

Transaction Expenses. For the six months ended June 25, 2005, we incurred \$0.2 million in costs related to an acquisition that was not consummated. For the six months ended June 26, 2004, we incurred transaction expenses of \$0.7 million related to the sale of Mattress Gallery in May 2004.

Licensing Fees. For the six months ended June 25, 2005, licensing fees decreased \$0.2 million, or 3.9%, to \$4.9 million from \$5.1 million for the six months ended June 26, 2004. The decrease in licensing fees was primarily due to lower sales of licensed products by a domestic licensee for the six months ended June 25, 2005 compared to the six months ended June 26, 2004 partially offset by additional royalties identified through a sales audit of a domestic licensee.

Interest Expense, Net. For the six months ended June 25, 2005, interest expense increased \$3.4 million, or 15.5%, to \$25.4 million from \$22.0 million for the six months ended June 26, 2004. Interest expense increased due to higher LIBOR base rates on our senior credit facility, partially offset by lower average outstanding borrowings for the six months ended June 25, 2005 compared to the six months ended June 26, 2004.

Income Taxes. The combined estimated federal, state, and foreign effective income tax rate of 35.7% for the six months ended June 25, 2005 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 were recorded and (ii) state income tax expense. The combined estimated federal, state, and foreign effective income tax rate of 36.0% for the six

months ended June 26, 2004 differed from the federal statutory rate of 35.0% primarily due to (i) state tax rate benefits realized as a result of a decrease in the rate at which our U.S. deferred tax assets and liabilities were recorded; (ii) the tax effect of a valuation allowance increase for Sleep Country's net deferred tax assets; and (iii) state income tax expense.

Liquidity and Capital Resources

Our principal sources of cash to fund liquidity needs are (i) cash provided by operating activities and (ii) borrowings available under our senior credit facility. Our primary use of funds consists of payments to fund working capital increases, principal and interest for our 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 our senior credit facility to be sufficient to meet our short-term and long-term liquidity needs.

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

	Six Months Ended	
	June 25, 2005	June 26, 2004
Statement of Cash Flow Data:		
Cash flows provided by (used in):		
Operating activities	\$ 18.5	\$ 38.2
Investing activities	(5.9)	(0.1)
Financing activities	(5.1)	(17.4)
Increase in cash and cash equivalents	7.5	20.7
Cash and cash equivalents:		
Beginning of period	23.9	3.7
End of period	<u>\$ 31.4</u>	<u>\$ 24.4</u>

Six Months Ended June 25, 2005 as Compared to Six Months Ended June 26, 2004

Cash flows provided by Operating Activities. For the six months ended June 25, 2005 compared to the six months ended June 26, 2004, our cash flows from operations decreased \$19.7 million primarily due to a \$6.3 million decline in net income combined with a \$6.5 million decrease in cash provided by working capital changes.

Cash flows used in Investing Activities. For the six months ended June 25, 2005 compared to the six months ended June 26, 2004, our cash flows used in investing activities increased \$5.8 million. Our first six months 2005 uses included \$3.3 million of contingent consideration paid related to the Juvenile Acquisition and capital expenditures of \$2.6 million, \$4.1 million less than in the first six months of 2004. Our capital expenditures were higher in 2004 primarily due to our opening a new manufacturing facility in Hazleton, PA during the second quarter. Our 2004 cash flows from investing activities benefited from \$6.5 million

received from the sale of Mattress Gallery.

Cash flows used in Financing Activities. For the six months ended June 25, 2005 compared to the six months ended June 26, 2004, our cash flows used in financing activities decreased \$12.3 million due primarily to reduced principal payments of on our debt of \$12.9 million.

Debt

The terms of our senior credit facility required a mandatory prepayment of our tranche C term loan of \$3.7 million, based upon our Consolidated Excess Cash Flows (as defined in the senior credit facility) for the year ended December 25, 2004. This payment was made in March 2005. In addition, we voluntarily prepaid \$1.0 million of our tranche C term loan in June 2005. As a result of these prepayments, our next scheduled quarterly tranche C term loan principal payment will be in June 2006.

As of June 25, 2005, we had availability to borrow \$64.9 million under our revolving loan facility after giving effect to \$10.1 million that was reserved for our reimbursement obligations with respect to outstanding letters of credit. The weighted average interest rates per annum in effect as of June 25, 2005 for the tranche C term loan and senior unsecured term loan were 5.84% and 7.0%, respectively.

We have developed and implemented a policy to utilize extended Eurodollar contracts to minimize the impact of near term Eurodollar rate increases. For approximately \$325 million of the tranche C term loan and \$140 million of the senior unsecured term loan, we set the interest rate at the twelve month Eurodollar Rate on January 26, 2005, which fixed the Eurodollar Rate at 3.25% through January 26, 2006. To further address interest rate risk, we have an interest rate cap agreement for a notional amount of \$170 million which capped the Eurodollar Rate at 5.0% for the period of January 26, 2005 through January 26, 2006. The interest rate cap agreement has not been designated for hedge accounting and, accordingly, any changes in the fair value are recorded in interest expense. The fair value of the interest rate cap agreement is less than \$0.3 million. The execution of these debt instruments resulted in us fixing or capping the interest rate on approximately 87% of our floating rate debt as of June 25, 2005.

Our long-term obligations contain various financial tests and covenants. We were in compliance with such covenants as of June 25, 2005. However, if our operating results fall below current expectations, we may not be able to meet such covenants in future periods. If we 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. We may not be able to obtain such a waiver on a timely basis or at all. The most restrictive covenants relate to ratios of adjusted EBITDA to interest coverage (interest coverage ratio) and net debt to Adjusted EBITDA (leverage ratio), all as defined in the senior credit facility. There is also a maximum capital expenditure limitation in the senior credit facility. The minimum interest coverage ratio and maximum leverage ratio are computed based on our results for the last twelve months ended, adjusted for any acquisitions or dispositions. More specifically, the senior credit facility's covenants, as amended, require:

- a minimum interest coverage ratio, with compliance levels ranging from an interest coverage of no less than 2.30:1.00 from June 30, 2005 through December 31, 2005; 2.40:1.00 from March 31, 2006 through December 31, 2006; 2.55:1.00 from March 31, 2007 through 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 ending thereafter.
- A maximum leverage ratio, with compliance levels ranging from total leverage of no greater than 6.50:1.00 from June 30, 2005 through December 31, 2005; 6.00:1.00 from March 31, 2006 through June 30, 2006; 5.75:1.00 from September 30, 2006 through December 31, 2006; 5.00:1.00 from March 31, 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.
- 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 other events.

Adjusted EBITDA (as defined in the 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; the aggregate amount of the fees, costs and cash expenses paid by us in connection with the consummation of the Acquisition (including without limitation, bonus and option payments); 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 us 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 our minimum interest coverage and maximum leverage ratios under our senior credit facility as of June 25, 2005 (dollar amounts in millions, except ratios). The terms and related calculations are defined in our senior credit facility.

	June 25, 2005
Calculation of minimum cash interest coverage ratio:	
Twelve months ended Adjusted EBITDA(1)	<u>\$112,139</u>
Consolidated cash interest expense(2)	<u>\$ 44,926</u>
Actual interest coverage ratio(3)	2.50
Minimum permitted interest coverage ratio	2.30
Calculation of maximum leverage ratio:	
Consolidated indebtedness	<u>\$747,313</u>
Less: Cash and cash equivalents(4)	<u>30,000</u>
Net debt	<u>\$717,313</u>
Adjusted EBITDA(1)	<u>\$112,139</u>
Actual leverage ratio(5)	6.40
Maximum permitted leverage ratio	6.50

(1) Adjusted EBITDA for the twelve months ended June 25, 2005 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, certain litigation and insurance charges relating to previous periods, retail segment charges relating to previous periods, management fees, and other non-recurring/non-cash charges as permitted under our senior credit facility. Additionally, Adjusted EBITDA is adjusted to include the operating results of our Simmons Juvenile division as though we operated this division as of the beginning of the twelve months ended June 25, 2005.

(2) Consolidated cash interest expense, as defined in the senior credit facility, for the twelve months ended June 25, 2005, as follows (in millions):

Interest expense, net	\$47,170
Interest income	<u>114</u>
Gross interest expense	47,284
Less: Non-cash interest expense	<u>(2,358)</u>
	<u>\$44,926</u>

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

(4) Our senior credit facility permits a maximum of \$30.0 million of cash to be netted against our debt for purposes of this covenant computation. Actual cash at June 25, 2005 totaled \$31.4 million.

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

Off-Balance Sheet Arrangements

On December 15, 2004, our indirect parent, Simmons Company, completed a private placement of \$269.0 million of 10% senior discount notes due 2014 (the "Discount Notes") with an effective yield of 10.2%. The aggregate proceeds from the issuance of the Discount Notes was \$165.1 million. The proceeds from the offering were used to make a dividend distribution to Simmons Company class A stockholders and to pay certain expenses related to the sale and distribution of the Discount Notes. The Discount Notes 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. Simmons Company's ability to make payments on the Discount Notes is dependent on our earnings and distributions of funds to Simmons Company. As of June 25, 2005, the aggregate amount of Discount Notes outstanding was \$173.9 million, which is not reflected on our condensed consolidated balance sheet.

In connection with the sale of Mattress Gallery, we continue to guarantee approximately \$1.3 million of Mattress Gallery'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 June 25, 2005.

Seasonality/Other

For the past several years, there has not been significant seasonality to our wholesale bedding business. Our retail bedding business, which accounted for \$37.9 million, or 9.2%, of our consolidated net sales for the first six months of 2005, has historically experienced, and we expect will continue to experience, seasonal and quarterly fluctuations in net sales, operating income and Adjusted EBITDA. As is the case with many bedding retailers, our retail business is subject to seasonal influences, typically characterized by higher sales for the months of May through September, which impacts our second and third quarter financial results.

Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123 (Revised 2004), *Share-Based Payment*, ("SFAS 123R"). SFAS 123R requires that compensation cost relating to share-based payment transactions be recognized in financial statements based upon the fair value of the award. SFAS 123R eliminates the option to account for the cost of stock-based compensation using the intrinsic value method as allowed under APB Opinion No. 25, *Accounting for Stock Issued to Employees*. We are considered a non-public entity as defined by SFAS 123R. SFAS 123R is effective for non-public entities for fiscal years beginning after December 15, 2005. We expect to adopt SFAS 123R as of the beginning of our fiscal year 2006. We do not anticipate that SFAS 123R will have a material effect on our consolidated financial statements.

In December 2004, the Financial Accounting Standards Board issued SFAS No. 153, *Exchanges of Nonmonetary Assets – An Amendment of APB Opinion No. 29*, ("SFAS 153").

SFAS 153, in contrast to APB No. 29, requires exchanges of nonmonetary assets to be accounted for based on the fair market value of the assets exchanged, rather than at their historical cost. The provisions of SFAS 153 are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005 and companies must apply the standard prospectively. We expect to adopt SFAS 153 as of the beginning of fiscal year 2006 and do not anticipate that SFAS 153 will have a material effect on our consolidated financial statements.

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 and pricing pressures in the bedding industry;
- legal and regulatory requirements;
- the success of new products, including HealthSmart™, our new Beautyrest® premium priced products, our new Deep Sleep® products, and the Beautyrest® Caresse® products;
- our relationships with our major suppliers;
- fluctuations in costs of raw materials;
- our relationship with significant customers and licensees;
- our labor relations;
- departure of key personnel;
- our ability to achieve the expected benefits from the people realignment plans;
- encroachments on our intellectual property;
- product liability claims;
- the timing, cost and success of opening new manufacturing facilities;
- our level of indebtedness;
- interest rate risks;

- compliance with covenants in our debt agreements;
- future acquisitions;
- an increase in return rates; 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 25, 2004 is presented under Item 7A of our Annual Report on Form 10-K for the fiscal year ended December 25, 2004.

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, fuel 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 risk from changes in interest rates. In order to address this risk, the senior credit facility requires us to adopt interest rate protection measures on our variable rate indebtedness through December 19, 2005 such that 50% of our consolidated funded indebtedness is either fixed or protected.

We have developed and implemented a policy to utilize extended Eurodollar contracts to minimize the impact of near term Eurodollar rate increases. For approximately \$325 million of the tranche C term loan and \$140 million of the senior unsecured term loan, we set the interest rate at the twelve month Eurodollar Rate on January 26, 2005, which fixed the Eurodollar Rate at 3.25% through January 26, 2006. To further address interest rate risk, we have an interest rate cap agreement for a notional amount of \$170 million which capped the Eurodollar Rate at 5.0% for the period of January 26, 2005 through January 26, 2006. The interest rate cap agreement has

not been designated for hedge accounting and, accordingly, any changes in the fair value are recorded in interest expense. The fair value of the interest rate cap agreement is less than \$0.3 million. The execution of these debt instruments resulted in us fixing or capping the interest rate on approximately 87% of our floating rate debt as of June 25, 2005.

All other factors remaining unchanged, a hypothetical 10% increase or decrease in interest rates for one year on our variable rate financial instruments would not have a material impact on earnings during 2005, but would result in an additional \$3.7 million of interest expense in 2006.

Commodity Price Risks

The major raw materials that we purchase for production are wire, spring components, lumber, cotton, insulator pads, innersprings, 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 affected by supply and demand. In particular, many of our goods can be impacted by fluctuations in petrochemical and steel prices. Additionally, our distribution costs can be impacted by fluctuations in diesel fuel 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 J to the Condensed Consolidated Financial Statements, Part 1, Item 1 included herein.

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

- 3.1 Amended and Restated By-Laws of 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)

AMENDED AND RESTATED
BY-LAWS
OF
SIMMONS BEDDING COMPANY
(P/K/A SIMMONS COMPANY; P/K/A SIMMONS HOLDINGS, INC.)

(A DELAWARE CORPORATION)

ARTICLE I

Stockholders

SECTION 1. Annual Meetings. The annual meeting of stockholders for the election of directors and for the transaction of such other business as may properly come before the meeting shall be held each year at such date and time, within or without the State of Delaware, as the Board of Directors shall determine.

SECTION 2. Special Meetings. Special meetings of stockholders for the transaction of such business as may properly come before the meeting may be called by order of the Board of Directors or by stockholders holding together at least a majority of all the shares of the Corporation entitled to vote at the meeting, and shall be held at such date and time, within or without the State of Delaware, as may be specified by such order.

SECTION 3. Notice of Meetings. Written notice of all meetings of the stockholders shall be mailed or delivered to each stockholder not less than 10 nor more than 60 days prior to the meeting. Notice of any special meeting shall state in general terms the purpose or purposes for which the meeting is to be held.

SECTION 4. Stockholder Lists. The officer who has charge of the stock ledger of the Corporation shall prepare and make, at least 10 days before every meeting of stockholders, a complete list of the stockholders entitled to vote at the meeting, arranged in alphabetical order, and showing the address of each stockholder and the number of shares registered in the name of each stockholder. Such list shall be open to the examination of any stockholder, for any purpose germane to the meeting, either at a place within the city where the meeting is to be held, which place shall be specified in the notice of the meeting, or, if not so specified, at the place where the meeting is to be held. The list shall also be produced and kept at the time and place of the meeting during the whole time thereof, and may be inspected by any stockholder who is present.

The stock ledger shall be the only evidence as to who are the stockholders entitled to examine the stock ledger, the list required by this section or the books of the Corporation, or to vote in person or by proxy at any meeting of stockholders.

SECTION 5. Quorum. Except as otherwise provided by law or the Corporation's Certificate of Incorporation, a quorum for the transaction of business at any meeting of stockholders shall consist of the holders of record of a majority of the issued and outstanding shares of the capital stock of the Corporation entitled to vote at the meeting, present in person or by proxy. At all meetings of the stockholders at which a quorum is present, all matters, except as otherwise provided by law or the Certificate of Incorporation, shall be decided by the vote of the holders of a majority of the shares entitled to vote thereat present in person or by proxy. If there be no such quorum, the

holders of a majority of such shares so present or represented may adjourn the meeting from time to time, without further notice, until a quorum shall have been obtained. When a quorum is once present it is not broken by the subsequent withdrawal of any stockholder.

SECTION 6. Organization. Meetings of stockholders shall be presided over by the Chairman, if any, or if none or in the Chairman's absence the Vice-Chairman, if any, or if none or in the Vice-Chairman's absence the Chief Executive Officer, if any, or if none or in the Chief Executive Officer's absence the President, if any, or if none or in the President's absence a Vice-President, or, if none of the foregoing is present, by a chairman to be chosen by the stockholders entitled to vote who are present in person or by proxy at the meeting. The Secretary of the Corporation, or in the Secretary's absence an Assistant Secretary, shall act as secretary of every meeting, but if neither the Secretary nor an Assistant Secretary is present, the presiding officer of the meeting shall appoint any person present to act as secretary of the meeting.

SECTION 7. Voting; Proxies; Required Vote. (a) At each meeting of stockholders, every stockholder shall be entitled to vote in person or by proxy appointed by instrument in writing, subscribed by such stockholder or by such stockholder's duly authorized attorney-in-fact (but no such proxy shall be voted or acted upon after three years from its date, unless the proxy provides for a longer period), and, unless the Certificate of Incorporation provides otherwise, shall have one vote for each share of stock entitled to vote registered in the name of such stockholder on the books of the Corporation on the applicable record date fixed pursuant to these By-laws. At all elections of directors the voting may but need not be by ballot and a plurality of the votes cast there shall elect. Except as otherwise required by law or the Certificate of Incorporation, any other action shall be authorized by a majority of the votes cast.

(b) Any action required or permitted to be taken at any meeting of stockholders may, except as otherwise required by law or the Certificate of Incorporation, be taken without a meeting, without prior notice and without a vote, if a consent in writing, setting forth the action so taken, shall be signed by the holders of record of the issued and outstanding capital stock of the Corporation having a majority of votes that would be necessary to authorize or take such action at a meeting at which all shares entitled to vote thereon were present and voted, and the writing or writings are filed with the permanent records of the Corporation. Prompt notice of the taking of corporate action without a meeting by less than unanimous written consent shall be given to those stockholders who have not consented in writing.

SECTION 8. Inspectors. The Board of Directors, in advance of any meeting, may, but need not, appoint one or more inspectors of election to act at the meeting or any adjournment thereof. If an inspector or inspectors are not so appointed, the person presiding at the meeting may, but need not, appoint one or more inspectors. In case any person who may be appointed as an inspector fails to appear or act, the vacancy may be filled by appointment made by the directors in advance of the meeting or at the meeting by the person presiding thereat. Each inspector, if any, before entering upon the

discharge of his or her duties, shall take and sign an oath faithfully to execute the duties of inspector at such meeting with strict impartiality and according to the best of his ability. The inspectors, if any, shall determine the number of shares of stock outstanding and the voting power of each, the shares of stock represented at the meeting, the existence of a quorum, and the validity and effect of proxies, and shall receive votes, ballots or consents, hear and determine all challenges and questions arising in connection with the right to vote, count and tabulate all votes, ballots or consents, determine the result, and do such acts as are proper to conduct the election or vote with fairness to all stockholders. On request of the person presiding at the meeting, the inspector or inspectors, if any, shall make a report in writing of any challenge, question or matter determined by such inspector or inspectors and execute a certificate of any fact found by such inspector or inspectors.

ARTICLE II

Board of Directors

SECTION 1. General Powers. The business, property and affairs of the Corporation shall be managed by, or under the direction of, the Board of Directors.

SECTION 2. Qualification; Number; Term; Remuneration. (a) Each director shall be at least 18 years of age. A director need not be a stockholder, a citizen of the United States, or a resident of the State of Delaware. The number of directors constituting the entire Board shall be 2, or such larger number as may be fixed from time to time by action of the stockholders or Board of Directors, one of whom may be selected by the Board of Directors to be its Chairman. The use of the phrase "entire Board" herein refers to the total number of directors which the Corporation would have if there were no vacancies.

(b) Directors who are elected at an annual meeting of stockholders, and directors who are elected in the interim to fill vacancies and newly created directorships, shall hold office until the next annual meeting of stockholders and until their successors are elected and qualified or until their earlier resignation or removal.

(c) Directors may be paid their expenses, if any, of attendance at each meeting of the Board of Directors and may be paid a fixed sum for attendance at each meeting of the Board of Directors or a stated salary as director. No such payment shall preclude any director from serving the Corporation in any other capacity and receiving compensation therefor. Members of special or standing committees may be allowed like compensation for attending committee meetings.

SECTION 3. Quorum and Manner of Voting. Except as otherwise provided by law, a majority of the entire Board shall constitute a quorum. A majority of the directors present, whether or not a quorum is present, may adjourn a meeting from time to time to another time and place without notice. The vote of the majority of the

directors present at a meeting at which a quorum is present shall be the act of the Board of Directors.

SECTION 4. Places of Meetings. Meetings of the Board of Directors may be held at any place within or without the State of Delaware, as may from time to time be fixed by resolution of the Board of Directors, or as may be specified in the notice of meeting.

SECTION 5. Annual Meeting. Following the annual meeting of stockholders, the newly elected Board of Directors shall meet for the purpose of the election of officers and the transaction of such other business as may properly come before the meeting. Such meeting may be held without notice immediately after the annual meeting of stockholders at the same place at which such stockholders' meeting is held.

SECTION 6. Regular Meetings. Regular meetings of the Board of Directors shall be held at such times and places as the Board of Directors shall from time to time by resolution determine.

SECTION 7. Special Meetings. Special meetings of the Board of Directors shall be held whenever called by the Chairman of the Board, Chief Executive Officer or President or by a majority of the directors then in office.

SECTION 8. Notice of Meetings. A notice of the place, date and time and the purpose or purposes of each meeting of the Board of Directors shall be given to each director by mailing the same at least two days before the [special] meeting, or by telegraphing or telephoning the same or by delivering the same personally not later than the day before the day of the meeting.

SECTION 9. Organization. At all meetings of the Board of Directors, the Chairman, if any, or if none or in the Chairman's absence or inability to act the Chief Executive Officer, if any, or if none or in the Chief Executive Officer's absence or inability to act the President, or in the President's absence or inability to act any Vice-President who is a member of the Board of Directors, or in such Vice-President's absence or inability to act a chairman chosen by the directors, shall preside. The Secretary of the Corporation shall act as secretary at all meetings of the Board of Directors when present, and, in the Secretary's absence, the presiding officer may appoint any person to act as secretary.

SECTION 10. Resignation. Any director may resign at any time upon written notice to the Corporation and such resignation shall take effect upon receipt thereof by the Chief Executive Officer, President or Secretary, unless otherwise specified in the resignation. Any or all of the directors may be removed, with or without cause, by the holders of a majority of the shares of stock outstanding and entitled to vote for the election of directors.

SECTION 11. Vacancies. Unless otherwise provided in these By-laws, vacancies on the Board of Directors, whether caused by resignation, death, disqualification, removal, an increase in the authorized number of directors or otherwise, may be filled by the affirmative vote of a majority of the remaining directors, although less than a quorum, or by a sole remaining director, or at a special meeting of the stockholders, by the holders of shares entitled to vote for the election of directors.

SECTION 12. Action by Written Consent. Any action required or permitted to be taken at any meeting of the Board of Directors may be taken without a meeting if all the directors consent thereto in writing, and the writing or writings are filed with the minutes of proceedings of the Board of Directors.

ARTICLE III

Committees

SECTION 1. Appointment. From time to time the Board of Directors by a resolution adopted by a majority of the entire Board may appoint any committee or committees for any purpose or purposes, to the extent lawful, which shall have powers as shall be determined and specified by the Board of Directors in the resolution of appointment.

SECTION 2. Procedures, Quorum and Manner of Acting. Each committee shall fix its own rules of procedure, and shall meet where and as provided by such rules or by resolution of the Board of Directors. Except as otherwise provided by law, the presence of a majority of the then appointed members of a committee shall constitute a quorum for the transaction of business by that committee, and in every case where a quorum is present the affirmative vote of a majority of the members of the committee present shall be the act of the committee. Each committee shall keep minutes of its proceedings, and actions taken by a committee shall be reported to the Board of Directors.

SECTION 3. Action by Written Consent. Any action required or permitted to be taken at any meeting of any committee of the Board of Directors may be taken without a meeting if all the members of the committee consent thereto in writing, and the writing or writings are filed with the minutes of proceedings of the committee.

SECTION 4. Term; Termination. In the event any person shall cease to be a director of the Corporation, such person shall simultaneously therewith cease to be a member of any committee appointed by the Board of Directors.

ARTICLE IV

Officers

SECTION 1. Election and Qualifications. The Board of Directors shall elect the officers of the Corporation, which shall include a Chief Executive Officer and a Secretary, and may include, by election or appointment, a President, one or more Vice-Presidents (any one or more of whom may be given an additional designation of rank or function), a Treasurer and such Assistant Secretaries, such Assistant Treasurers and such other officers as the Board may from time to time deem proper. Each officer shall have such powers and duties as may be prescribed by these By-laws and as may be assigned by the Board of Directors, the Chief Executive Officer or the President.

SECTION 2. Term of Office and Remuneration. The term of office of all officers shall be one year and until their respective successors have been elected and qualified, but any officer may be removed from office, either with or without cause, at any time by the Board of Directors. Any vacancy in any office arising from any cause may be filled for the unexpired portion of the term by the Board of Directors. The remuneration of all officers of the Corporation may be fixed by the Board of Directors or in such manner as the Board of Directors shall provide.

SECTION 3. Resignation; Removal. Any officer may resign at any time upon written notice to the Corporation and such resignation shall take effect upon receipt thereof by the Chief Executive Officer, President or Secretary, unless otherwise specified in the resignation. Any officer shall be subject to removal, with or without cause, at any time by vote of a majority of the entire Board.

SECTION 4. Chairman of the Board. The Chairman of the Board of Directors, if there be one, shall preside at all meetings of the Board of Directors and shall have such other powers and duties as may from time to time be assigned by the Board of Directors.

SECTION 5. Chief Executive Officer. The chief executive officer shall have such duties as customarily pertain to that office, including the implementation of the policies of the Corporation as determined by the Board of Directors, and shall have such other authority as from time to time may be assigned by the Board of Directors.

SECTION 6. President. The Board of Directors may designate a President. The President shall have such duties as customarily pertain to that office, including the general management and supervision of the property, business and affairs of the Corporation and shall have such other authority as from time to time may be assigned by the Board of Directors.

SECTION 7. Vice-President. A Vice-President may execute and deliver in the name of the Corporation contracts and other obligations and instruments pertaining to the regular course of the duties of said office, and shall have such other authority as

from time to time may be assigned by the Board of Directors, the President or the Chief Executive Officer.

SECTION 8. Treasurer. The Treasurer shall in general have all duties incident to the position of Treasurer and such other duties as may be assigned by the Board of Directors, the President or the Chief Executive Officer.

SECTION 9. Secretary. The Secretary shall in general have all the duties incident to the office of Secretary and such other duties as may be assigned by the Board of Directors, the President or the Chief Executive Officer.

SECTION 10. Assistant Officers. Any assistant officer shall have such powers and duties of the officer such assistant officer assists as such officer or the Board of Directors shall from time to time prescribe.

ARTICLE V

Books and Records

SECTION 1. Location. The books and records of the Corporation may be kept at such place or places within or outside the State of Delaware as the Board of Directors or the respective officers in charge thereof may from time to time determine. The record books containing the names and addresses of all stockholders, the number and class of shares of stock held by each and the dates when they respectively became the owners of record thereof shall be kept by the Secretary as prescribed in the By-laws and by such officer or agent as shall be designated by the Board of Directors.

SECTION 2. Addresses of Stockholders. Notices of meetings and all other corporate notices may be delivered personally or mailed to each stockholder at the stockholder's address as it appears on the records of the Corporation.

SECTION 3. Fixing Date for Determination of Stockholders of Record. (a) In order that the Corporation may determine the stockholders entitled to notice of or to vote at any meeting of stockholders or any adjournment thereof, the Board of Directors may fix a record date which record date shall not be more than 60 nor less than 10 days before the date of such meeting. If no record date is fixed by the Board of Directors, the record date for determining stockholders entitled to notice of or to vote at a meeting of stockholders shall be at the close of business on the day next preceding the day on which notice is given, or, if notice is waived, at the close of business on the day next preceding the day on which the meeting is held. A determination of stockholders of record entitled to notice of or to vote at a meeting of stockholders shall apply to any adjournment of the meeting; provided, however, that the Board of Directors may fix a new record date for the adjourned meeting.

(b) In order that the Corporation may determine the stockholders entitled to consent to corporate action in writing without a meeting, the Board of

Directors may fix a record date which date shall not be more than 10 days after the date upon which the resolution fixing the record date is adopted by the Board of Directors. If no record date has been fixed by the Board of Directors, the record date for determining stockholders entitled to consent to corporate action in writing without a meeting, when no prior action by the Board of Directors is required, shall be the first date on which a signed written consent setting forth the action taken or proposed to be taken is delivered to the Corporation by delivery to its registered office in this State, its principal place of business, or an officer or agent of the Corporation having custody of the book in which proceedings of meetings of stockholders are recorded. Delivery made to the Corporation's registered office shall be by hand or by certified or registered mail, return receipt requested. If no record date has been fixed by the Board of Directors and prior action by the Board of Directors is required by this chapter, the record date for determining stockholders entitled to consent to corporate action in writing without a meeting shall be at the close of business on the day on which the Board of Directors adopts the resolution taking such prior action.

(c) In order that the Corporation may determine the stockholders entitled to receive payment of any dividend or other distribution or allotment of any rights or the stockholders entitled to exercise any rights in respect of any change, conversion or exchange of stock, or for the purpose of any other lawful action, the Board of Directors may fix a record date which record date shall be not more than 60 days prior to such action. If no record date is fixed, the record date for determining stockholders for any such purpose shall be at the close of business on the day on which the Board of Directors adopts the resolution relating thereto.

ARTICLE VI

Certificates Representing Stock

SECTION 1. Certificates; Signatures. The shares of the Corporation shall be represented by certificates, provided that the Board of Directors of the Corporation may provide by resolution or resolutions that some or all of any or all classes or series of its stock shall be uncertificated shares. Any such resolution shall not apply to shares represented by a certificate until such certificate is surrendered to the Corporation. Notwithstanding the adoption of such a resolution by the Board of Directors, every holder of stock represented by certificates and upon request every holder of uncertificated shares shall be entitled to have a certificate, signed by or in the name of the Corporation by the Chairman or Vice-Chairman of the Board of Directors, or the President or Vice-President, and by the Treasurer or an Assistant Treasurer, or the Secretary or an Assistant Secretary of the Corporation, representing the number of shares registered in certificate form. Any and all signatures on any such certificate may be facsimiles. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer, transfer agent or registrar before such certificate is issued, it may be issued by the Corporation with the same effect as if he were such officer, transfer agent or registrar at the date of issue. The name of the

holder of record of the shares represented thereby, with the number of such shares and the date of issue, shall be entered on the books of the Corporation.

SECTION 2. Transfers of Stock. Upon compliance with provisions restricting the transfer or registration of transfer of shares of stock, if any, shares of capital stock shall be transferable on the books of the Corporation only by the holder of record thereof in person, or by duly authorized attorney, upon surrender and cancellation of certificates for a like number of shares, properly endorsed, and the payment of all taxes due thereon.

SECTION 3. Fractional Shares. The Corporation may, but shall not be required to, issue certificates for fractions of a share where necessary to effect authorized transactions, or the Corporation may pay in cash the fair value of fractions of a share as of the time when those entitled to receive such fractions are determined, or it may issue scrip in registered or bearer form over the manual or facsimile signature of an officer of the Corporation or of its agent, exchangeable as therein provided for full shares, but such scrip shall not entitle the holder to any rights of a stockholder except as therein provided.

The Board of Directors shall have power and authority to make all such rules and regulations as it may deem expedient concerning the issue, transfer and registration of certificates representing shares of the Corporation.

SECTION 4. Lost, Stolen or Destroyed Certificates. The Corporation may issue a new certificate of stock in place of any certificate, theretofore issued by it, alleged to have been lost, stolen or destroyed, and the Board of Directors may require the owner of any lost, stolen or destroyed certificate, or his legal representative, to give the Corporation a bond sufficient to indemnify the Corporation against any claim that may be made against it on account of the alleged loss, theft or destruction of any such certificate or the issuance of any such new certificate.

ARTICLE VII

Dividends

Subject always to the provisions of law and the Certificate of Incorporation, the Board of Directors shall have full power to determine whether any, and, if any, what part of any, funds legally available for the payment of dividends shall be declared as dividends and paid to stockholders; the division of the whole or any part of such funds of the Corporation shall rest wholly within the lawful discretion of the Board of Directors, and it shall not be required at any time, against such discretion, to divide or pay any part of such funds among or to the stockholders as dividends or otherwise; and before payment of any dividend, there may be set aside out of any funds of the Corporation available for dividends such sum or sums as the Board of Directors from time to time, in its absolute discretion, thinks proper as a reserve or reserves to meet contingencies, or for equalizing dividends, or for repairing or maintaining any property of the Corporation, or for such other purpose as the Board of Directors shall think conducive

to the interest of the Corporation, and the Board of Directors may modify or abolish any such reserve in the manner in which it was created.

ARTICLE VIII

Ratification

Any transaction, questioned in any law suit on the ground of lack of authority, defective or irregular execution, adverse interest of director, officer or stockholder, non-disclosure, miscomputation, or the application of improper principles or practices of accounting, may be ratified before or after judgment, by the Board of Directors or by the stockholders, and if so ratified shall have the same force and effect as if the questioned transaction had been originally duly authorized. Such ratification shall be binding upon the Corporation and its stockholders and shall constitute a bar to any claim or execution of any judgment in respect of such questioned transaction.

ARTICLE IX

Fiscal Year

The fiscal year of the Corporation shall be fixed, and shall be subject to change, by the Board of Directors. Unless otherwise fixed by the Board of Directors, the fiscal year of the Corporation shall be the calendar year.

ARTICLE X

Waiver of Notice

Whenever notice is required to be given by these By-laws or by the Certificate of Incorporation or by law, a written waiver thereof, signed by the person or persons entitled to said notice, whether before or after the time stated therein, shall be deemed equivalent to notice.

ARTICLE XI

Bank Accounts, Drafts, Contracts, Etc.

SECTION 1. Bank Accounts and Drafts. In addition to such bank accounts as may be authorized by the Board of Directors, the primary financial officer or any person designated by said primary financial officer, whether or not an employee of the Corporation, may authorize such bank accounts to be opened or maintained in the name and on behalf of the Corporation as he may deem necessary or appropriate, payments from such bank accounts to be made upon and according to the check of the Corporation in accordance with the written instructions of said primary financial officer, or other person so designated by the Treasurer.

SECTION 2. Contracts. The Board of Directors may authorize any person or persons, in the name and on behalf of the Corporation, to enter into or execute and deliver any and all deeds, bonds, mortgages, contracts and other obligations or instruments, and such authority may be general or confined to specific instances.

SECTION 3. Proxies; Powers of Attorney; Other Instruments. The Chairman, the Chief Executive Officer, the President or any other person designated by any of them shall have the power and authority to execute and deliver proxies, powers of attorney and other instruments on behalf of the Corporation in connection with the rights and powers incident to the ownership of stock by the Corporation. The Chairman, the Chief Executive Officer, the President or any other person authorized by proxy or power of attorney executed and delivered by any of them on behalf of the Corporation may attend and vote at any meeting of stockholders of any company in which the Corporation may hold stock, and may exercise on behalf of the Corporation any and all of the rights and powers incident to the ownership of such stock at any such meeting, or otherwise as specified in the proxy or power of attorney so authorizing any such person. The Board of Directors, from time to time, may confer like powers upon any other person.

SECTION 4. Financial Reports. The Board of Directors may appoint the primary financial officer or other fiscal officer and/or the Secretary or any other officer to cause to be prepared and furnished to stockholders entitled thereto any special financial notice and/or financial statement, as the case may be, which may be required by any provision of law.

ARTICLE XII

Amendments

The Board of Directors shall have power to adopt, amend or repeal By-laws. By-laws adopted by the Board of Directors may be repealed or changed, and new By-laws made, by the stockholders, and the stockholders may prescribe that any By-law made by them shall not be altered, amended or repealed by the Board of Directors.

CERTIFICATIONS

CHIEF EXECUTIVE OFFICER'S SECTION 302 CERTIFICATION

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

1. I have reviewed this Quarterly Report on Form 10-Q of Simmons Bedding 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 9, 2005

/s/ Charles R. Eitel

Name: Charles R. Eitel

Title: Chief Executive Officer

CHIEF FINANCIAL OFFICER'S SECTION 302 CERTIFICATION

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

1. I have reviewed this Quarterly Report on Form 10-Q of Simmons Bedding 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 9, 2005

/s/ William S. Creekmuir

Name: William S. Creekmuir
Title: Chief Financial Officer

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 Bedding 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 June 25, 2005 (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 9, 2005

/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 Bedding Company and will be retained by Simmons Bedding Company and furnished to the Securities and Exchange Commission or its staff upon request.

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 Bedding 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 June 25, 2005 (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 9, 2005

/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 Bedding Company and will be retained by Simmons Bedding Company and furnished to the Securities and Exchange Commission or its staff upon request.