

SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

Filing Date: **2004-08-12** | Period of Report: **2004-07-03**  
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FILER

**SELECT COMFORT CORP**

CIK: **827187** | IRS No.: **410157886** | State of Incorpor.: **MN** | Fiscal Year End: **1231**  
Type: **10-Q** | Act: **34** | File No.: **000-25121** | Film No.: **04967909**  
SIC: **2510** Household furniture

Business Address  
6105 TRENTON LANE NORTH  
MINNEAPOLIS MN 55442  
7635517000

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

FORM 10-Q

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

For the Quarterly Period Ended July 3, 2004

COMMISSION FILE NO. 0-25121

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SELECT COMFORT CORPORATION  
(Exact name of registrant as specified in its charter)

MINNESOTA  
(State or other jurisdiction of  
incorporation or organization)

41-1597886  
(I.R.S. Employer  
Identification No.)

6105 TRENTON LANE NORTH  
MINNEAPOLIS, MINNESOTA  
(Address of principal executive offices)

55442  
(Zip code)

Registrant's telephone number, including area code: (763) 551-7000

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES[X] NO[ ]

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). YES[X] NO[ ]

As of July 3, 2004, 36,671,441 shares of Common Stock of the Registrant were outstanding.

SELECT COMFORT CORPORATION  
AND SUBSIDIARIES

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PART I: FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS  
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SELECT COMFORT CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE AMOUNTS)

<S>	<C>	<C>
	(UNAUDITED) JULY 3, 2004	JANUARY 3, 2004
	-----	-----
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 29,167	\$ 24,725
Marketable securities - current (note 2)	14,127	49,322
Accounts receivable, net of allowance for doubtful accounts of \$704 and \$619	9,133	6,823
Inventories (note 3)	14,312	12,381
Prepaid expenses	7,776	5,244
Deferred tax assets	6,672	6,039
	-----	-----
Total current assets	81,187	104,534
Marketable securities - non-current (note 2)	44,778	1,071
Property and equipment, net	40,114	36,134

Deferred tax assets	6,298	5,620
Other assets	3,650	3,343
	-----	-----
Total assets	\$ 176,027	\$150,702
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 21,962	\$ 14,773
Consumer prepayments	6,952	5,970
Accruals:		
Sales returns	4,053	3,469
Compensation and benefits	11,918	16,579
Taxes and withholding	3,095	3,661
Other	5,379	6,110
	-----	-----
Total current liabilities	53,359	50,562
Accrued warranty costs	1,905	2,557
Other liabilities	5,174	4,821
	-----	-----
Total liabilities	60,438	57,940
	-----	-----
Shareholders' equity (notes 4 and 5):		
Undesignated preferred stock; 5,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, \$.01 par value; 95,000,000 shares authorized, 36,671,441 and 35,769,606 shares issued and outstanding, respectively	367	358
Additional paid-in capital	114,742	104,085
Unearned compensation	(1,974)	(877)
Retained earnings (accumulated deficit)	2,454	(10,804)
	-----	-----
Total shareholders' equity	115,589	92,762
	-----	-----
Total liabilities and shareholders' equity	\$ 176,027	\$150,702
	=====	=====

See accompanying notes to consolidated financial statements.

</TABLE>

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<TABLE>

SELECT COMFORT CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS  
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)  
(UNAUDITED)

<S>	<C>		<C>	
	THREE MONTHS ENDED		SIX MONTHS ENDED	
	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003
	-----	-----	-----	-----
Net sales	\$124,720	\$101,993	\$264,683	\$203,951
Cost of sales	47,806	38,920	101,735	76,977
	-----	-----	-----	-----
Gross profit	76,914	63,073	162,948	126,974

Operating expenses:				
Sales and marketing	57,638	46,284	121,358	95,201
General and administrative	10,050	9,209	20,684	17,510
Store closings and asset impairments	-	(15)	-	59
Total operating expenses	67,688	55,478	142,042	112,770
Operating income	9,226	7,595	20,906	14,204
Other income (expense):				
Interest income	340	137	652	250
Interest expense	-	(53)	-	(141)
Other, net	-	-	-	24
Other income (expense), net	340	84	652	133
Income before income taxes	9,556	7,679	21,558	14,337
Income tax expense	3,683	2,918	8,300	5,448
Net income	\$ 5,883	\$ 4,761	\$ 13,258	\$ 8,889
Net income per share (note 4) - basic	\$ 0.16	\$ 0.15	\$ 0.37	\$ 0.28
Weighted average shares - basic	36,547	32,018	36,304	31,449
Net income per share (note 4) - diluted	\$ 0.15	\$ 0.12	\$ 0.33	\$ 0.23
Weighted average shares - diluted	40,236	38,778	40,101	38,492

See accompanying notes to consolidated financial statements.

</TABLE>

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<TABLE>

SELECT COMFORT CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)  
(UNAUDITED)

<S>

<C>

<C>

SIX MONTHS ENDED

	JULY 3, 2004	JUNE 28, 2003
Cash flows from operating activities:		
Net income	\$ 13,258	\$ 8,889
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,741	5,155
Amortization of debt discount and deferred finance fees	-	130
Non-cash compensation	183	30
Loss on disposal of assets and impaired assets	-	59

Deferred tax (benefit) expense	(1,311)	4,806
Change in operating assets and liabilities:		
Accounts receivable, net	(2,310)	(2,900)
Inventories	(1,931)	(1,866)
Prepaid expenses	(2,532)	424
Other assets	(324)	(10)
Accounts payable	7,189	4,147
Accrued sales returns	584	174
Accrued compensation and benefits	(4,661)	(3,152)
Accrued taxes and withholding	4,177	(233)
Consumer prepayments	982	2,417
Other accruals and liabilities	(1,030)	227
	-----	-----
Net cash provided by operating activities	19,015	18,297
	-----	-----
Cash flows from investing activities:		
Purchases of property and equipment	(10,704)	(10,313)
Investments in marketable securities	(54,768)	(17,706)
Proceeds from maturity of marketable securities	46,256	14,717
	-----	-----
Net cash used in investing activities	(19,216)	(13,302)
	-----	-----
Cash flows from financing activities:		
Principal payments on debt	-	(11)
Repurchase of common stock	(240)	(1,834)
Proceeds from issuance of common stock	4,883	2,376
	-----	-----
Net cash provided by financing activities	4,643	531
	-----	-----
Increase in cash and cash equivalents	4,442	5,526
Cash and cash equivalents, at beginning of period	24,725	27,176
	-----	-----
Cash and cash equivalents, at end of period	\$ 29,167	\$ 32,702
	=====	=====

See accompanying notes to consolidated financial statements.

</TABLE>

SELECT COMFORT CORPORATION AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) BASIS OF FINANCIAL STATEMENT PRESENTATION

The consolidated financial statements for the three months and six months ended July 3, 2004 of Select Comfort Corporation and subsidiaries ("Select Comfort" or the "Company"), have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission and reflect, in the opinion of management, all normal recurring adjustments necessary to present fairly the financial position of the Company as of July 3, 2004 and January 3, 2004 and the results of operations and cash flows for the periods presented.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although management believes the disclosures are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with the Company's most recent audited consolidated financial statements and related notes included in the Company's Annual Report to Shareholders and its Form 10-K for the fiscal year ended January 3, 2004. Operating results for the Company on a quarterly basis may not be indicative of operating results for the full year.

No additional new accounting pronouncements have been issued that are expected to have a material effect on the Company's financial results.

(2) MARKETABLE SECURITIES

The Company invests its cash in highly liquid debt instruments issued by the US government and related agencies, municipalities and in corporate notes and commercial paper issued by companies with investment grade ratings. The Company's investments have an original maturity of up to 36 months with an average time to maturity of 18 months as of July 3, 2004. Investments with an original maturity of less than 90 days are classified as cash equivalents. Investments with an original maturity of greater than 90 days are classified as marketable securities. Marketable securities with a remaining maturity of greater than one year are classified as long-term. The Company's marketable securities are classified as held-to-maturity and are carried at amortized cost. Marketable securities held at July 3, 2004 carried an amortized cost of \$44.8 million and a fair value of \$44.3 million.

(3) INVENTORIES

<TABLE>

Inventories consist of the following (in thousands):

<S>	<C>	<C>
	JULY 3, 2004	JANUARY 3, 2004
	-----	-----
Raw materials	\$ 3,795	\$ 3,715
Work in progress	122	123
Finished goods	10,395	8,543
	-----	-----
	\$14,312	\$12,381
	=====	=====

</TABLE>

SELECT COMFORT CORPORATION AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(4) NET INCOME PER COMMON SHARE

The following computations reconcile reported net income with net income available to common shareholders per share-basic and diluted (in thousands, except per share amounts):

<TABLE>

<S>	<C>	<C>	<C>	<C>	<C>	<C>
	THREE MONTHS ENDED			SIX MONTHS ENDED		
JULY 3, 2004	NET	WEIGHTED	PER	NET	WEIGHTED	PER
-----	INCOME	AVERAGE	SHARE	INCOME	AVERAGE	SHARE
	-----	SHARES	AMOUNT	-----	SHARES	AMOUNT
	-----	-----	-----	-----	-----	-----
Net income	\$ 5,883			\$ 13,258		
BASIC EPS						
Net income available to common shareholders	5,883	36,547	\$ 0.16	13,258	36,304	\$ 0.37
			=====			=====

EFFECT OF DILUTIVE SECURITIES

Options	-	2,334	-	2,427		
Common stock warrants	-	1,355	-	1,370		
<hr/>						
DILUTED EPS						
Net income available to common shareholders plus assumed conversions	\$ 5,883	40,236	\$ 0.15	\$ 13,258	40,101	\$ 0.33
<hr/>						
	THREE MONTHS ENDED			SIX MONTHS ENDED		
	WEIGHTED AVERAGE SHARES		PER SHARE AMOUNT	WEIGHTED AVERAGE SHARES		PER SHARE AMOUNT
JUNE 28, 2003						
	NET INCOME			NET INCOME		
<hr/>						
Net income	\$ 4,761			\$ 8,889		
<hr/>						
BASIC EPS						
Net income available to common shareholders	4,761	32,018	\$ 0.15	8,889	31,449	\$ 0.28
<hr/>						
EFFECT OF DILUTIVE SECURITIES						
Options	-	2,613	-	2,481		
Common stock warrants	-	3,787	-	4,019		
Convertible debt	27	360		81	543	
<hr/>						
DILUTED EPS						
Net income available to common shareholders plus assumed conversions	\$ 4,788	38,778	\$ 0.12	\$ 8,970	38,492	\$ 0.23
<hr/>						

</TABLE>

Additional potentially dilutive securities totaling 28,000 and 54,000 for the three- and six-month periods ended July 3, 2004 and 643,000 and 631,000 for the three- and six-month periods ended June 28, 2003, have been excluded from diluted EPS because these securities' exercise price was greater than the average market price of the Company's common shares.

#### (5) STOCK AND STOCK OPTION INCENTIVES

The Company uses the intrinsic value method of accounting for stock options. Under this method no compensation cost has been recognized in the consolidated financial statements for employee stock option grants or the discount feature of the Company's employee stock purchase plan.

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#### SELECT COMFORT CORPORATION AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Had the Company determined compensation cost based on the fair value at the grant date for its stock options and employee stock purchase plan under an alternative accounting method, the Company's net income would have been adjusted as outlined below (in thousands, except per share amounts):

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003



Net income, as reported	\$ 5,883	\$ 4,761	\$13,258	\$ 8,889
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(760)	(729)	(1,434)	(1,376)
Pro forma net income	\$ 5,123	\$ 4,032	\$11,824	\$ 7,513
Income per share				
Basic - as reported	\$ 0.16	\$ 0.15	\$ 0.37	\$ 0.28
Basic - pro forma	\$ 0.14	\$ 0.13	\$ 0.33	\$ 0.24
Diluted - as reported	\$ 0.15	\$ 0.12	\$ 0.33	\$ 0.23
Diluted - pro forma	\$ 0.13	\$ 0.10	\$ 0.29	\$ 0.20

</TABLE>

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

<TABLE>

<S>

	<C>		<C>	
	THREE MONTHS ENDED		SIX MONTHS ENDED	
	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003
Expected dividend yield.....	0%	0%	0%	0%
Expected stock price volatility.....	55%	90%	55%	90%
Risk-free interest rate.....	2.0%	2.0%	2.0%	2.0%
Expected life in years.....	3.6	3.6	3.6	3.6
Weighted-average fair value at grant date..	\$10.22	\$9.13	\$10.41	\$6.04

</TABLE>

The Company issued restricted stock awards to certain employees in conjunction with its stock-based compensation plan. The shares vest between five and ten years from the date of issuance based on continued employment. Compensation expense related to restricted stock awards is based upon the market price at date of grant and is charged to earnings on a straight-line basis over the vesting period. 153,500 shares of restricted stock were outstanding as of July 3, 2004. Total compensation expense related to restricted stock was \$183,000 and \$30,000 for the six month period ended July 3, 2004 and June 28, 2003, respectively.

#### (6) LITIGATION

On August 13, 2003, a lawsuit was filed against the Company in Superior Court of the State of California, County of Ventura. The suit was subsequently amended on September 18, 2003. This suit was filed by two former store managers alleging misclassification of employment position and seeking class certification. The complaint seeks judgment for unpaid overtime compensation alleged to exceed \$1.0 million, together with related penalties, restitution, attorneys' fees and costs. We are investigating the allegations in the complaint and intend to vigorously defend this litigation. As this case is in the early stages of discovery, the financial impact to the Company, if any, cannot be predicted.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, any losses that may occur from these other matters are adequately covered by insurance or are provided for in the consolidated financial statements and the ultimate outcome of these other matters will not have a material effect on the consolidated financial position or results of operations of the Company.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

THE FOLLOWING DISCUSSION AND ANALYSIS SHOULD BE READ IN CONJUNCTION WITH THE CONSOLIDATED FINANCIAL STATEMENTS AND THE NOTES THERETO INCLUDED HEREIN. THIS QUARTERLY REPORT ON FORM 10-Q CONTAINS FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995. YOU CAN IDENTIFY FORWARD-LOOKING STATEMENTS BY THOSE THAT ARE NOT HISTORICAL IN NATURE, PARTICULARLY THOSE THAT USE TERMINOLOGY SUCH AS "MAY," "WILL," "SHOULD," "EXPECTS," "ANTICIPATES," "CONTEMPLATES," "ESTIMATES," "BELIEVES," "PLANS," "PROJECTS," "PREDICTS," "POTENTIAL" OR "CONTINUE" OR THE NEGATIVE OF THESE OR SIMILAR TERMS. THESE STATEMENTS ARE SUBJECT TO CERTAIN RISKS AND UNCERTAINTIES THAT COULD CAUSE ACTUAL RESULTS TO DIFFER MATERIALLY FROM THE COMPANY'S HISTORICAL EXPERIENCE AND ITS PRESENT EXPECTATIONS OR PROJECTIONS. IMPORTANT FACTORS KNOWN TO SELECT COMFORT THAT COULD CAUSE SUCH MATERIAL DIFFERENCES ARE IDENTIFIED AND DISCUSSED IN PART I, ITEM 1 OF OUR ANNUAL REPORT ON FORM 10-K FOR THE FISCAL YEAR ENDED JANUARY 3, 2004, WHICH DISCUSSION IS INCORPORATED HEREIN BY REFERENCE. THESE IMPORTANT FACTORS INCLUDE:

- o GENERAL AND INDUSTRY ECONOMIC TRENDS,
- o UNCERTAINTIES ARISING FROM DOMESTIC AND GLOBAL EVENTS,
- o CONSUMER CONFIDENCE AND SPENDING,
- o THE EFFECTIVENESS AND EFFICIENCY OF OUR ADVERTISING AND PROMOTIONAL EFFORTS,
- o ADVERTISING RATES AND THE VOLATILITY OF ADVERTISING RATES DURING THE OLYMPIC GAMES AND ELECTION SEASON,
- o CONSUMER ACCEPTANCE OF OUR PRODUCTS AND SLEEP TECHNOLOGY,
- o INDUSTRY COMPETITION,
- o OUR ABILITY TO SECURE SUITABLE RETAIL LOCATIONS,
- o WARRANTY EXPENSES,
- o CALIFORNIA WAGE AND HOUR LITIGATION,
- o OUR DEPENDENCE ON SIGNIFICANT SUPPLIERS OR SINGLE SOURCES OF SUPPLY,
- o THE VULNERABILITY OF ANY SUPPLIERS TO RECESSIONARY PRESSURES, LIQUIDITY CONCERNS OR OTHER FACTORS,
- o GOVERNMENTAL REGULATION, INCLUDING ANTICIPATED FUTURE REGULATION OF DIRECT MARKETING TELEPHONE SOLICITATIONS AND BEDDING FLAMMABILITY STANDARDS,
- o INFLATION OF COMMODITY OR DELIVERY COSTS, AND
- o RISKS AND UNCERTAINTIES DETAILED FROM TIME TO TIME IN THE COMPANY'S FILINGS WITH THE SEC, INCLUDING THE COMPANY'S ANNUAL REPORT ON FORM 10-K AND OTHER PERIODIC REPORTS FILED WITH THE SEC.

THE COMPANY HAS NO OBLIGATION TO PUBLICLY UPDATE OR REVISE ANY OF THE FORWARD-LOOKING STATEMENTS CONTAINED IN THIS QUARTERLY REPORT ON FORM 10-Q.

OVERVIEW AND CRITICAL ACCOUNTING POLICIES

Select Comfort(R) is the leading developer, manufacturer and marketer of premium-quality, adjustable-firmness beds. The air-chamber technology of our proprietary Sleep Number bed allows adjustable firmness on each side of the mattress and provides a sleep surface that is clinically proven to provide better sleep quality and greater relief of back pain compared to traditional mattress products. In addition we market and sell accessories and other sleep related products which focus on providing personalized comfort to complement the Sleep Number bed and provide a better night's sleep to the consumer.

We generate revenue by selling our products through four complementary distribution channels. Three of these channels: retail, direct marketing and e-commerce, are company-controlled and sell directly to consumers. Our wholesale channel sells to leading home furnishings retailers, specialty bedding retailers and the QVC shopping channel.

The proportion of our total net sales, by dollar volume, from each of our channels is summarized as follows:

<TABLE>

<S>	<C>	<C>	<C>	<C>
	Three Months Ended	Six Months Ended		
	7/3/04	6/28/03	7/3/04	6/28/03

Stores	77%	77%	77%	78%
Direct Call Center	12%	13%	12%	13%
E-commerce	5%	4%	5%	4%
Wholesale	6%	6%	6%	5%

The growth rates of each distribution channel are as follows:

<S>	<C>		<C>	
	Three Months Ended		Six Months Ended	
	7/3/04	6/28/03	7/3/04	6/28/03
Channel	Channel	Channel	Channel	
	inc(dec)	inc(dec)	inc(dec)	inc(dec)
Retail:				
Comparable store sales	14%	34%	20%	32%
New/closed stores, net	8%	4%	8%	3%
Retail total	22%	38%	28%	35%
Direct marketing	13%	17%	20%	15%
E-commerce	32%	23%	43%	26%
Wholesale	34%	6%	75%	(8)%

The number of company-operated retail locations is summarized as follows:

<S>	<C>		<C>	
	Three Months Ended		Six Months Ended	
	7/3/04	6/28/03	7/3/04	6/28/03
Beginning of period	351	323	344	322
Opened	12	10	21	12
Closed	(3)	(1)	(5)	(2)
End of period	360	332	360	332

We anticipate opening 9 new retail stores during the remainder of 2004. We do not anticipate closing any additional stores in 2004. However the term of our agreement with Bed, Bath & Beyond, representing 13 stores in leased departments, expires August 31, 2004 and we are currently evaluating the extension of this arrangement. These stores represented less than 2% of revenue in 2003.

Our growth plans are centered on increasing the awareness of our products and stores through expansion of media, increasing distribution - primarily through new retail store openings, and expanding and improving our product lines. Our primary market consists of consumers in the U.S. domestic market.

On May 21, 2004, we entered into an agreement with Radisson Hotels. We expect revenue over the contract term of \$40 million to \$60 million with ultimate revenues dependent upon order volumes from individual Radisson franchisees. While we expect margins from these incremental sales to be in the single digits, we believe the added exposure to consumers provides an opportunity for additional incremental sales through our existing higher margin channels.

In August 2004 a local Minneapolis news story reported the potential for mold formation within our mattresses. Consumer response to these reports could impact future sales trends and warranty costs. Our response to customer calls resulting from this story has increased our warranty costs by approximately \$60,000 to date. Historically, warranty claims associated with mold have affected less than

1% of our customer base annually at an annual cost of less than \$200,000. While we believe our warranty reserves are adequate to address this issue, we will continue to monitor claims activity and make future adjustments to our warranty reserves, if appropriate.

Increases in sales, along with controlling costs, have provided significant improvement to operating income and operating margin over the past several years. The majority of operating margin improvement has been generated through leverage in selling expenses (increased sales through the existing store base) and leverage of our existing infrastructure (general and administrative expenses). We expect any future improvements in operating margin to be derived from similar sources. Our target is to sustain sales growth rates of 15% to 25% and sustain earnings growth rates of approximately 30%.

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## RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated, the Company's results of operations expressed as dollars and percentages of net sales. Figures are in millions except per share amounts.

	THREE MONTHS ENDED		THREE MONTHS ENDED		SIX MONTHS ENDED		SIX MONTHS ENDED	
	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003
Net sales	\$124.7	100.0%	\$102.0	100.0%	\$264.7	100.0%	\$204.0	100.0%
Cost of sales	47.8	38.3%	38.9	38.2%	101.7	38.4%	77.0	37.7%
Gross profit	76.9	61.7%	63.1	61.8%	162.9	61.6%	127.0	62.3%
Operating expenses:								
Sales and marketing	57.6	46.2%	46.3	45.4%	121.4	45.9%	95.2	46.7%
General and administrative	10.0	8.1%	9.2	9.0%	20.7	7.8%	17.5	8.6%
Store closings and asset impairments	0.0	0.0%	0.0	0.0%	0.0	0.0%	0.1	0.0%
Total operating expenses	67.7	54.3%	55.5	54.4%	142.0	53.7%	112.8	55.3%
Operating income	9.2	7.4%	7.6	7.4%	20.9	7.9%	14.2	7.0%
Other income (expense), net	0.3	0.3%	0.1	0.1%	0.7	0.2%	0.1	0.1%
Income before income taxes	9.6	7.7%	7.7	7.5%	21.6	8.1%	14.3	7.1%
Income tax expense	3.7	3.0%	2.9	2.8%	8.3	3.1%	5.4	2.7%
Net income	5.9	4.7%	\$ 4.8	4.7%	\$ 13.3	5.0%	\$ 8.9	4.4%

</TABLE>

	THREE MONTHS ENDED		THREE MONTHS ENDED		SIX MONTHS ENDED		SIX MONTHS ENDED	
	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003	JULY 3, 2004	JUNE 28, 2003
Net income per share:								
Basic	\$ 0.16	\$ 0.15	\$ 0.37	\$ 0.28				
Diluted	\$ 0.15	\$ 0.12	\$ 0.33	\$ 0.23				
Weighted-average number of common shares:								
Basic	36.5	32.0	36.3	31.4				
Diluted	40.2	38.8	40.1	38.5				

</TABLE>

## NET SALES

We record revenue at the time product is shipped to our customer, except when beds are delivered and set up by our home delivery employees, in which case revenue is recorded at the time the bed is delivered and set up in the home. We

reduce sales at the time revenue is recognized for estimated returns. This estimate is based on historical return rates, which are reasonably consistent from period to period. If actual returns vary from expected rates, revenue in future periods is adjusted, which could have a material adverse effect on future results of operations. Historically we have not experienced material adjustments to the financial statements due to changes to these estimates.

#### COST OF SALES

Cost of sales includes costs associated with purchasing materials, manufacturing costs and costs to deliver our products to our customers. Cost of sales also includes estimated costs to service warranty claims of customers. This estimate is based on historical claim rates during the warranty period. Because this estimate covers an extended period of time, a revision of estimated claim rates could result in a significant adjustment of estimated future costs of fulfilling warranty commitments. An increase in estimated claim rates could have a material adverse effect on future results of operations. Historically we have not experienced material adjustments to the financial statements due to changes to these estimates.

#### GROSS PROFIT

Our gross profit margin is dependent on a number of factors and may fluctuate from quarter to quarter. These factors include the mix of products sold, the level at which we offer promotional discounts to purchase our products, the cost of materials, delivery and manufacturing and the mix of sales between wholesale and company-controlled distribution channels. Sales of products manufactured by third parties, such as accessories and our adjustable foundation, generate lower gross margins. Similarly, sales directly to consumers through company-controlled channels generally generate higher gross margins than sales through our wholesale channels because we capture both the manufacturer's and retailer's margin.

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#### SALES AND MARKETING EXPENSES

Sales and marketing expenses include advertising and media production, other marketing and selling materials such as brochures, videos, customer mailings and in-store signage, sales compensation, store occupancy costs and customer service. We expense all store opening and advertising costs as incurred, except for production costs and advance payments, which are deferred and expensed from the time the advertisement is first run. Advertising expense was \$18.8 million and \$40.3 million for the three and six months ended July 3, 2004 as compared to \$12.7 million and \$27.3 million for the three and six months ended June 28, 2003. Future advertising expenditures will depend on the effectiveness and efficiency of the advertising in creating awareness of our products and brand name, generating consumer inquiries and driving consumer traffic to our points of sale.

#### GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses include costs associated with management of functional areas, including information technology, human resources, finance, sales and marketing administration, investor relations, risk management and research and development. Costs include salaries, bonus and benefits, information hardware, software and maintenance, office facilities, insurance, shareholder relations costs and other overhead.

#### STORE CLOSINGS AND ASSET IMPAIRMENTS

Store closing and asset impairment expenses include charges made against operating expenses for store related or other capital assets that have been written-off when a store is underperforming and generating negative cash flows. We evaluate our long-lived assets, including leaseholds and fixtures in existing stores and stores expected to be remodeled, based on expected cash flows through the remainder of the lease term after considering the potential impact of planned operational improvements and marketing programs. Expected cash flows may not be realized, which could cause long-lived assets to become impaired in future periods and could have a material adverse effect on future results of operations. Store assets are written off when we believe these costs will not be

recovered through future operations.

#### QUARTERLY AND ANNUAL RESULTS

Quarterly and annual operating results may fluctuate significantly as a result of a variety of factors, including increases or decreases in comparable store sales, the timing, amount and effectiveness of advertising expenditures, any changes in sales return rates or warranty experience, the timing of new store openings and related expenses, net sales contributed by new stores, competitive factors, any disruptions in supplies or third-party service providers and general economic conditions, seasonality of sales and timing of QVC shows and wholesale sales and consumer confidence. Furthermore, a substantial portion of net sales is often realized in the last month of a quarter, due in part to our promotional schedule and commission structure. As a result, we may be unable to adjust spending in a timely manner, and our business, financial condition and operating results may be significantly harmed. Our historical results of operations may not be indicative of the results that may be achieved for any future period.

#### COMPARISON OF THREE MONTHS ENDED JULY 3, 2004 WITH THREE MONTHS ENDED JUNE 28, 2003

##### NET SALES

Net sales increased 22% to \$124.7 million for the three months ended July 3, 2004 from \$102.0 million for the three months ended June 28, 2003, due to a 10% increase in mattress unit sales and higher average selling prices. The average selling price per bed set in our company controlled channels was \$1,867, an increase of approximately 13% over second quarter last year. The higher average selling price resulted primarily from growth in unit sales at higher price points and a decline in unit sales at lower price points. The increase in mattress unit sales was driven predominately by sales from new stores and by sales to wholesale partners while the growth rate of units within same stores slowed in comparison to prior periods.

The increase in net sales by sales channel was attributable to (i) a \$17.6 million increase in sales from our retail stores, including an increase in comparable store sales of \$10.8 million and an increase of \$6.8 million from new stores, net of stores closed, (ii) a \$1.8 million increase in direct marketing sales, (iii) a \$1.4 million increase in sales through the Company's e-commerce channel and (iv) a \$2.0 million increase in sales from the Company's wholesale channel.

##### GROSS PROFIT

Gross profit decreased to 61.7% for the three months ended July 3, 2004 from 61.8% for the three months ended June 28, 2003, primarily due to increases in gross margins resulting from sales of higher priced bed models, offset by decreases in gross margin attributable to increased sales of adjustable foundations, increased utilization of our home delivery services and channel mix.

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##### SALES AND MARKETING EXPENSES

Sales and marketing expenses increased 24% to \$57.6 million for the three months ended July 3, 2004 from \$46.3 million for the three months ended June 28, 2003 and increased as a percentage of net sales to 46.2% from 45.4% for the comparable prior-year period. The \$11.3 million increase was primarily due to additional media investments, sales-based incentive compensation, and increased occupancy costs. The increase as a percentage of net sales was comprised primarily of a 2.6 percentage point (ppt) increase in media investments offset by a 1.8 ppt leverage of fixed costs (occupancy, base sales compensation and certain marketing expenses) over higher sales. With additional sales growth, we expect sales and marketing expenses as a percentage of net sales to decline as we achieve greater leverage from our base sales compensation and occupancy costs while reinvesting some of these leverage benefits into higher levels of media investments and training.

#### GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative (G&A) expenses increased 9% to \$10.0 million for the three months ended July 3, 2004 from \$9.2 million for the three months ended June 28, 2003 but decreased as a percentage of net sales to 8.1% from 9.0% for the prior-year period. The dollar increase in G&A was comprised primarily of increased compensation and benefits expenses related to additional headcount and from additional depreciation from infrastructure investments. We expect G&A growth rates to continue to be lower than the rate of sales growth due to leveraging the fixed component of G&A expenses across a higher sales base.

#### OTHER INCOME (EXPENSE), NET

Other income (expense) increased \$256,000 to \$340,000 for the three months ended July 3, 2004 from \$84,000 for the three months ended June 28, 2003. The improvement is primarily due to increased interest income reflecting higher balances of invested cash.

#### INCOME TAX EXPENSE

Income tax expense increased \$0.8 million to \$3.7 million for the three months ended July 3, 2004 from \$2.9 million for the three months ended June 28, 2003. The effective tax rate was 38.5% in 2004 and 38.0% in 2003.

#### COMPARISON OF SIX MONTHS ENDED JULY 3, 2004 WITH SIX MONTHS ENDED JUNE 28, 2003

##### NET SALES

Net sales increased 30% to \$264.7 million for the six months ended July 3, 2004 from \$204.0 million for the six months ended June 28, 2003, due to a 17% increase in mattress unit sales and higher average selling prices. The average selling price per bed set in our company controlled channels was \$1,839, an increase of approximately 14% over the six month average selling price last year. The higher average selling price resulted primarily from growth in unit sales at higher price points and a decline in unit sales at lower price points. The increase in mattress unit sales was driven predominately by sales from new stores, and by sales to QVC and other wholesale partners while the growth rate of units within same stores slowed in comparison to prior periods.

The increase in net sales by sales channel was attributable to (i) a \$44.5 million increase in sales from our retail stores, including an increase in comparable store sales of \$30.7 million and an increase of \$13.8 million from new stores, net of stores closed, (ii) a \$5.6 million increase in direct marketing sales, (iii) a \$3.6 million increase in sales through the Company's e-commerce channel and (iv) a \$7.1 million increase in sales from the Company's wholesale channel.

##### GROSS PROFIT

Gross profit decreased to 61.6% for the six months ended July 3, 2004 from 62.3% for the six months ended June 28, 2003, primarily due to increases in gross margins resulting from sales of higher priced bed models, offset by decreases in gross margin attributable to increased sales of adjustable foundations, channel mix, and increased utilization of our home delivery services.

##### SALES AND MARKETING EXPENSES

Sales and marketing expenses increased 28% to \$121.4 million for the six months ended July 3, 2004 from \$95.2 million for the six months ended June 28, 2003 and decreased as a percentage of net sales to 45.9% from 46.7% for the comparable prior-year period. The \$26.2 million increase was primarily due to additional media investments, sales-based incentive compensation, and increased occupancy costs. The decrease as a percentage of net sales was comprised primarily of a 1.9 percentage point (ppt) increase in media investments offset by a 2.7 ppt leverage of fixed costs (occupancy, base sales compensation and certain marketing expenses) over higher sales.

#### GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative (G&A) expenses increased 18% to \$20.7 million for the six months ended July 3, 2004 from \$17.5 million for the six months ended June



28, 2003 but decreased as a percentage of net sales to 7.8% from 8.6% for the prior-year period. The dollar increase in G&A was comprised primarily of increased compensation and benefits expenses related to additional headcount and from additional depreciation from infrastructure investments.

#### STORE CLOSINGS AND ASSET IMPAIRMENT EXPENSES

Store closing and asset impairment expense decreased from a \$59,000 expense for the six months ended June 28, 2003 to \$0 for the six months ended July 3, 2004. In 2003, the entire \$59,000 expense represents impairments related to store closures.

#### OTHER INCOME (EXPENSE), NET

Other income (expense) increased \$519,000 to \$652,000 for the six months ended July 3, 2004 from \$133,000 for the six months ended June 28, 2003. The improvement is primarily due to increased interest income reflecting higher balances of invested cash.

#### INCOME TAX EXPENSE

Income tax expense increased \$2.9 million to \$8.3 million for the six months ended July 3, 2004 from \$5.4 million for the six months ended June 28, 2003. The effective tax rate was 38.5% in 2004 and 38.0% in 2003.

#### LIQUIDITY AND CAPITAL RESOURCES

As of July 3, 2004, we had cash and marketable securities of \$88.1 million, \$43.3 million classified as a current asset. As of January 3, 2004, cash and marketable securities totaled \$75.1 million, \$74.0 million classified as current. Net working capital totaled \$27.8 million as of July 3, 2004 compared to \$54.0 million for 2003. The decrease in net working capital was due to a shift to longer-term investments which are reported as non-current assets. The \$13.0 million improvement in cash balances was the result of generating \$8.3 million of operating free cash flow (\$19.0 million of cash provided by operating activities, reduced by \$10.7 million of capital expenditures) and \$4.6 million of cash provided by financing activities. Cash from financing activities was primarily comprised of cash received from option and warrant exercises and shares purchased by employees as part of an employee share purchase program, offset by purchases of stock made by us as part of our ongoing common stock repurchase program. We expect to continue to generate positive cash flows from operations in the future, while not anticipating any significant additional working capital requirements due to our advantaged business model which requires low levels of inventory and other working capital assets.

We generated cash from operations for the six months ended July 3, 2004 and June 28, 2003 of \$19.0 million and \$18.3 million, respectively. The \$0.7 million year-to-year improvement in cash from operations resulted primarily from improved operating income in 2004 largely offset by increases in income taxes paid, reflecting the utilization of substantially all net operating loss carryforwards ("NOLs") in 2003.

Capital expenditures amounted to \$10.7 million for the six months ended July 3, 2004, compared to \$10.3 million for the six months ended June 28, 2003. In both periods our capital expenditures related primarily to new and remodeled retail stores and investments in information technology. The majority of the year over year increase in capital expenditures relates to investments in retail stores. In the first half of 2004 we opened 21 retail stores, while in the first half of 2003 we opened 12 stores. We anticipate opening 9 additional stores in 2004 while completing the marquee and design upgrade of approximately 130 stores by the end of the third quarter. We will fund the investment in new and upgraded stores with cash on hand and cash generated from operations. We expect our new stores to be cash flow positive within the first 12 months of operation and, as a result, do not anticipate a negative effect on net cash provided by operations.

Net cash provided by financing activities totaled \$4.6 million for the six months ended July 3, 2004, compared to \$0.5 million for the six months ended June 28, 2003. The \$4.1 million increase in cash from financing activities was comprised of an increase of \$2.5 million received for exercises of stock options and warrants and for employee purchases of common stock and a \$1.6 million



decrease in purchases of common stock by us under our board-authorized common stock repurchase program. During the third quarter of 2004 (through August 10, 2001) we used approximately \$14.6 million dollars for the repurchase of shares under this program. Additional purchases of Select Comfort stock may be made from time-to-time, subject to market conditions and at prevailing market prices, through open market purchases. Repurchased shares will be retired and may be reissued in the future for general corporate or other purposes. We may terminate or limit the stock repurchase program at any time.

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Management believes that cash generated from operations will be a sufficient source of liquidity for the short- and long- term and should provide adequate capital for capital expenditures and common stock repurchases, if any. In addition, our advantaged business model, which can operate with minimal working capital, does not require significant additional capital to fund operations. In 2003 we obtained a \$15 million bank revolving line of credit to provide additional cash flexibility in the case of unexpected significant external or internal developments. The line of credit is a three-year senior secured revolving facility. The interest rate on borrowings is calculated using LIBOR plus 1.50% to 2.25% with the incremental rate dependent on our leverage ratio, as defined by the lender. We are subject to certain financial covenants under the agreement, principally consisting of minimum liquidity requirements, working capital and leverage ratios. We have remained in full compliance with the financial covenants from the date the agreement was originated. We currently have no borrowings outstanding under this credit agreement.

#### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. Predicting future events is inherently an imprecise activity and as such requires the use of judgment. Actual results may vary from estimates in amounts that may be material to the financial statements. The accounting policies discussed below are considered critical because changes to certain judgments and assumptions inherent in these policies could materially affect the financial statements.

Our critical accounting policies relate to revenue recognition, accrued sales returns, accrued warranty costs and impairment of long-lived assets and long-lived assets to be disposed of by us.

In certain instances, accounting principles generally accepted in the United States of America allow for the selection of alternative accounting methods. Our significant policy that involves the selection of an alternative method is accounting for stock options.

#### STOCK-BASED COMPENSATION

Two alternative methods exist for accounting for stock options: the intrinsic value method and the fair value method. We use the intrinsic value method of accounting for stock options, and accordingly, no compensation expense has been recognized in the financial statements for options granted to employees, or for the discount feature of our employee stock purchase plan.

#### REVENUE RECOGNITION

We record revenue at the time product is shipped to our customer, except when beds are delivered and set up by our home delivery employees, in which case revenue is recorded at the time the bed is delivered and set up in the home.

#### ACCRUED SALES RETURNS

We reduce sales at the time revenue is recognized for estimated returns. This estimate is based on historical return rates, which are reasonably consistent from period to period. If actual returns vary from expected rates, revenue in future periods is adjusted, which could have a material adverse effect on future

results of operations.

#### ACCRUED WARRANTY COSTS

The estimated costs to service warranty claims of customers is included in cost of sales. This estimate is based on historical claim rates during the warranty period. Because this estimate covers an extended period of time, a revision of estimated claim rates could result in a significant adjustment of estimated future costs of fulfilling warranty commitments. An increase in estimated claim rates could have a material adverse effect on future results of operations.

#### STORE CLOSING AND ASSET IMPAIRMENT EXPENSES

We evaluate our long-lived assets, including leaseholds and fixtures in existing stores, based on expected cash flows through the remainder of the lease term after considering the potential impact of planned operational improvements and marketing programs. Expected cash flows may not be realized, which could cause

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long-lived assets to become impaired in future periods and could have a material adverse effect on future results of operations. Store assets are written off when we believe these costs will not be recovered through future operations.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of investments. The counterparties to our investments consist of government agencies and various major corporations of investment-grade credit standing. The Company does not believe there is significant risk of non-performance by these counterparties because the Company limits the amount of credit exposure to any one financial institution and any one type of investment.

In addition, our investments carry fixed interest rates which, in an increasing interest rate environment, would result in unrealized losses in our investment portfolio. The Company limits this interest rate risk by designating this portfolio as "held-to-maturity" and by managing the short-term liquidity needs of the business by matching investment duration to liquidity needs.

#### ITEM 4. DISCLOSURE CONTROLS AND PROCEDURES

As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of our President and Chief Executive Officer, and our Senior Vice President and Chief Financial Officer, of our disclosure controls and procedures. Based on this evaluation, these officers concluded that our disclosure controls and procedures are effective in recording, processing, summarizing and reporting information necessary to satisfy our disclosure obligations under the Securities Exchange Act of 1934.

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#### PART II: OTHER INFORMATION

##### ITEM 1. LEGAL PROCEEDINGS

On August 13, 2003, a lawsuit was filed against the Company in Superior Court of the State of California, County of Ventura. The suit was subsequently amended on September 18, 2003. This suit was filed by two former store managers alleging misclassification of employment position and seeking class certification. The complaint seeks judgment for unpaid overtime compensation alleged to exceed \$1.0 million, together with related penalties, restitution, attorneys' fees and costs. We are investigating the allegations in the complaint and intend to

vigorously defend this litigation. As this case is in the early stages of discovery, the financial impact to the Company, if any, cannot be predicted.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, any losses that may occur from these other matters are adequately covered by insurance or are provided for in the consolidated financial statements and the ultimate outcome of these other matters will not have a material effect on the consolidated financial position or results of operations of the Company.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

(a) - (d) Not applicable.

(e) Registrant Purchases of Equity Securities

<S>	<C>	<C>	<C>	<C>
Period	(a) Total Number of Shares (or Units) Purchased (1)	(b) Average Price Paid per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (2)	(d) Maximum Number (or Approximate Dollar Value) of shares (or Units) that May Yet Be Purchased Under the Plans or Programs
April 4, 2004 - May 1, 2004	177	\$28.23	-	\$14,991,000
May 2, 2004 - May 29, 2004	457	20.15	-	16,464,000
May 30, 2004 - July 3, 2004	161	17.66	-	15,344,000
Total	795	\$21.44	-	

(1) Includes 795 shares acquired in open market transactions by the administrator of the Company's non-qualified deferred compensation plan in order to accommodate investment elections of plan participants.

(2) In February 2003, the Company announced that the Board of Directors had authorized the use of up to \$12.5 million for the repurchase of shares of the Company's common stock. This authorization was subsequently modified to allow for the use of a formula specified amount based on certain minimum cash levels, for the repurchase of shares. The Audit Committee of the Board of Directors reviews, on a quarterly basis, the authority granted as well as any repurchases under this program. This authorization is currently not subject to expiration.

During the period from July 4, 2004 through August 10, 2004, the Company repurchased approximately 793,000 shares at a total cost of approximately \$14.6 million.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Our Annual Meeting of Shareholders was held on May 20, 2004. The

following individuals were elected as Directors of the Company at the Annual Meeting to serve for terms of three years expiring at the 2007 Annual Meeting of Shareholders or until their successors are elected and qualified. Shares voted in favor of these Directors and shares withheld were as follows:

Thomas J. Albani

Shares For	32,030,677
Shares Withheld	2,169,274

David T. Kollat

Shares For	33,067,008
Shares Withheld	1,132,943

William R. McLaughlin

Shares For	33,472,862
Shares Withheld	727,089

In addition to the Directors named above, the following Directors' terms continued after the Annual Meeting and will expire at the Annual Meeting of Shareholders in the year indicated below:

Name	Term Expires
Christopher P. Kirchen	2005
Brenda J. Lauderback	2005
Michael A. Peel	2005
Jean-Michel Valette	2005
Patrick A. Hopf	2006
Trudy A. Rautio	2006
Ervin R. Shames	2006

Shareholders approved the adoption of the 2004 Stock Incentive Plan. Shares voted in favor and against the plan were as follows:

Shares For	20,254,407
Shares Against	8,789,706

Shareholders also approved the appointment of KPMG LLP, certified public accountants, as independent auditors for the fiscal year ending January 1, 2005. Shares voted in favor and against this appointment were as follows:

Shares For	33,485,767
Shares Against	147,126

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) EXHIBITS.

EXHIBIT NUMBER	DESCRIPTION
10.1	Exclusive Supplier Agreement between Radisson Hotels International, Inc. and Select Comfort Corporation.*
10.2	Select Comfort Corporation 2004 Stock Incentive Plan.
31.1	Certification of CEO pursuant to Section 302 of

- 31.2 the Sarbanes-Oxley Act of 2002.  
Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of CEO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.
- 32.2 Certification of CFO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.

\*Portions of this Exhibit have been omitted pursuant to a request for confidential treatment.

(b) REPORTS ON FORM 8-K

During the quarter ended July 3, 2004, Current Reports on Form 8-K consisted of the following:

- (i) Current Report furnished under Item 12 of Form 8-K on April 9, 2004, announcing preliminary sales for the first quarter ended April 3, 2004.
- (ii) Current Report furnished under Item 12 of Form 8-K on April 20, 2004, announcing results for the first quarter ended April 3, 2004 and earnings guidance for second quarter 2004.
- (iii) Current Report furnished under Item 7 and 9 of Form 8-K on May 11, 2004, providing slides that were presented at an analyst day on May 10, 2004.
- (iv) Current Report furnished under Item 9 of Form 8-K on May 21, 2004, announcing election of president and chief executive officer to the additional position of chairman of the board and announcing results of the annual shareholder meeting held May 20, 2004.
- (v) Current Report furnished under Item 9 of Form 8-K on May 25, 2004, announcing exclusive brand agreement with Carlson Hotels Worldwide.

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SELECT COMFORT CORPORATION

/s/ William R. McLaughlin

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William R. McLaughlin  
President and Chief Executive Officer  
(principal executive officer)

August 11, 2004

/s/ James C. Raabe

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James C. Raabe  
Senior Vice President and Chief  
Financial Officer  
(principal financial and accounting  
officer)

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EXHIBIT INDEX

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32.2	Certification of CFO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.

\*Portions of this Exhibit have been omitted pursuant to a request for confidential treatment.

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## Certification by Chief Executive Officer

I, William R. McLaughlin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Select Comfort Corporation;
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 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 we 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 (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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 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 11, 2004

/s/ William R. McLaughlin

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William R. McLaughlin  
President and Chief Executive Officer



## Certification by Chief Financial Officer

I, James C. Raabe, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Select Comfort Corporation;
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 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 we 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 (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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 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 11, 2004

/s/ James C. Raabe

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James C. Raabe  
Senior Vice President and Chief  
Financial Officer

CERTIFICATION PURSUANT TO  
18 U.S.C. ss.1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Select Comfort Corporation (the "Company") on Form 10-Q for the period ended July 3, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, William R. McLaughlin, President and Chief Executive Officer of the Company, solely for the purposes of 18 U.S.C. ss.1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, does hereby certify that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ William R. McLaughlin

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William R. McLaughlin  
President and Chief Executive Officer  
August 11, 2004

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

CERTIFICATION PURSUANT TO  
18 U.S.C. ss.1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Select Comfort Corporation (the "Company") on Form 10-Q for the period ended July 3, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, James C. Raabe, Senior Vice President and Chief Financial Officer of the Company, solely for the purposes of 18 U.S.C. ss.1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, does hereby certify that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

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

/s/ James C. Raabe

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James C. Raabe  
Senior Vice President and Chief  
Financial Officer  
August 11, 2004

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

EXCLUSIVE SUPPLIER AGREEMENT

BETWEEN

RADISSON HOTELS INTERNATIONAL, INC.

&

SELECT COMFORT CORPORATION

EFFECTIVE DATE: MAY 21, 2004

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

This Exclusive Supplier Agreement (the "Agreement"), dated May 21 2004 (the "Effective Date"), is by and between Select Comfort Corporation, a Minnesota corporation whose address for notice purposes is Attention: General Counsel, 6105 Trenton Lane North, Minneapolis, MN 55442 Fax No.: (763) 551-6888 ("Select Comfort") and Radisson Hotels International, Inc., a Delaware corporation whose address for notice purposes is c/o Legal Department, 701 Carlson Parkway, Mail Stop 8256, Minneapolis, MN 55305 Fax No.: (763) 212-1080 ("Radisson").

RECITALS

- A. Select Comfort is a developer, manufacturer and marketer of adjustable-firmness beds, selling a proprietary line of beds under the Sleep Number(R) brand that feature adjustable air chamber mattresses (the "Beds").
- B. Radisson owns the Radisson Marks and the System, and owns, operates, or is a franchiser of the Hotels.
- C. Radisson desires to contract with Select Comfort as its supplier of the Beds and certain other bed products, and Select Comfort desires to contract with Radisson as its exclusive lodging industry provider for the Beds, pursuant to the terms of this Agreement.
- D. Terms used in this Agreement with initial capital letters shall have the meanings assigned to such terms in Section 15.26 hereof or the meanings otherwise assigned to such terms by this Agreement.

NOW THEREFORE, for good and adequate consideration, the receipt and sufficiency of which are hereby acknowledged and in consideration of the mutual obligations set forth below, the parties agree as follows:

#### ARTICLE 1 - TERM

##### 1.1. TERM OF THE AGREEMENT

The term of this Agreement (the "Term") shall commence on the Effective Date and continue until the date of termination of the exclusivity provisions set forth in Section 2.2 hereof. Notwithstanding the foregoing, the provisions of Articles 7, 8, 12, 13, 14 and 15 hereof, and of Sections 4.2 and 4.3 hereof, shall survive the termination of this Agreement and will continue to govern the rights and obligations of the parties hereto indefinitely following the termination of this Agreement.

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#### ARTICLE 2 - EXCLUSIVITY

##### 2.1. SELECT COMFORT EXCLUSIVITY

During the Term of this Agreement and as long as Select Comfort is not in material breach of this Agreement, Radisson agrees to (a) establish the installation of the Beds as a System Standard for all hotel rooms in the Radisson System and (b) to use its reasonable business efforts to encourage the adoption of the Beds in the Radisson System with the goal of achieving installation of no less than XXX Beds by December 31, 2006. Radisson's reasonable business efforts shall include, at a minimum, the following activities undertaken in good faith and designed to achieve the foregoing distribution goal:

- o Radisson will promote the Beds at the upcoming and future Annual Business Conferences for the Radisson System and in all similar meetings or similar opportunities with franchisees in the Radisson System;
- o Radisson will strongly encourage adoption of the Beds by the Radisson Franchise Advisory Council, which advises the Radisson System regarding the adoption of new System Standards;
- o Radisson will contribute funds to install and promote the Beds in a select number of the Hotels in key distribution markets. As a part of this obligation, in addition to the Beds already installed in the nine (9) test locations, Radisson agrees to fund the purchase and installation of four (4) Beds per property in the Radisson System by the end of 2004.

Select Comfort acknowledges that Radisson, as a franchisor of the System, does not directly control the purchasing activities of franchisee hotels and is subject to various Legal Requirements regarding substantial changes to the System. Accordingly, for purposes of this Agreement, Radisson does not guarantee the adoption by the Hotels of any specific percentage of the Beds by any precise date. However, Radisson does represent and warrant that it will carry out the above-referenced plan and that it is authorized under applicable franchise agreements to establish the Beds as a System Standard for all hotel rooms in the Radisson System. Radisson further represents that there are currently an aggregate of 251 Hotels in the Radisson System, with an aggregate of approximately 60,279 hotel rooms that use approximately 91,700 beds.

2.2. RADISSON EXCLUSIVITY

During the periods described below and as long as Radisson is not in material breach of this Agreement, Radisson will have the exclusive right to the use of the Beds within the hotel and interval/timeshare industry as follows:

A. SALES AND MARKETING IN HOTEL AND INTERVAL/TIMESHARE INDUSTRY. Except as specifically provided in this Agreement, Select Comfort shall not sell any beds (including the Beds) to, or conduct marketing programs promoting any beds with, any Person for use in the hotel or

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interval/timeshare industry, commencing on the Effective Date and through December 31, 2008 (the "Exclusivity"). However, Select Comfort may (upon reasonable prior notice from Select Comfort to Radisson, and with an opportunity for discussion of the matter at a periodic review meeting as contemplated by this Agreement or in any similar meeting): (i) continue to service and sell bed products and services (including the Beds) to Persons for use in the hotel or interval/timeshare industry to which Select Comfort has previously sold beds and who are identified on Exhibit 2.2A, attached hereto and made a part hereof, and (ii) service and sell bed products and services (including the Beds) to other independent hotel or interval/timeshare industry customers, so long as any such independent hotel or timeshare industry customer as of the time of the initial sale does not consist of more than XXX separate properties operating under a common hotel or interval/timeshare name. Notwithstanding the above, the Hotels collectively must meet the following minimum requirements in order to maintain the Exclusivity:

1. By December 31, 2005, the Hotels must have ordered, purchased and installed at least XXX Beds; and
2. By December 31, 2006, the Hotels must have ordered, purchased and installed at least an additional XXX Beds.

If the Hotels fail to meet the above requirements for any reason other than due to: (i) Select Comfort's failure to meet its production capabilities as represented by Select Comfort in this Agreement; or (ii) a material breach of this Agreement by Select Comfort, Select Comfort may terminate the Exclusivity, effective immediately upon written notice thereof to Radisson given on or before February 28, 2006 in the case of a failure to meet the requirement set forth in Section 2.2.A.1 above, and by February 28, 2007 in the case of a failure to meet the requirement set forth in Section 2.2.B.2 above.

B. SALES AND MARKETING TO EXCEPTIONAL CATEGORY OF HOTEL AND INTERVAL/TIMESHARE INDUSTRY. At any time during the Term of this Agreement, Carlson properties and/or cruise ships that compete in the Exceptional Category of the hotel or interval/timeshare industry may purchase and install Beds under the terms of this Agreement. On or after July 1, 2007, Select Comfort may service and sell bed products and services (including the Beds), on a non-exclusive basis, to any Person in the Exceptional Category of the hotel or interval/timeshare industry. Select Comfort will offer to Carlson properties and/or cruise ships, on a non-exclusive basis, a similar program as Select Comfort may offer to other customers in the Exceptional Category, provided that the Carlson opportunity represents comparable volume potential for Select Comfort versus an alternative brand.

C. RADISSON'S RIGHT TO EXTEND EXCLUSIVITY. Radisson shall have the

option to extend the Exclusivity beyond December 31, 2008 as follows:

1. If the Hotels have ordered and purchased at least XXX Beds by December 31, 2006, and installed at least ninety percent (90%)

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of that number by such date (and, installed the full number by February 28, 2007), Radisson's Exclusivity will automatically be extended through December 31, 2009; and

2. If the Hotels and/or Radisson's Affiliates have ordered and purchased a total of at least XXX Beds by December 31, 2009, and installed at least ninety percent (90%) of that number by such date (and, installed the full number by February 28, 2010), Radisson's Exclusivity will automatically be extended through December 31, 2010.

For the avoidance of doubt, Beds that are ordered, purchased and installed by Hotels which thereafter leave the Radisson System during the term of this Agreement will count and be applied toward all rights and minimum requirements set forth herein.

#### ARTICLE 3 - MARKETING OBLIGATIONS AND PERIODIC REVIEW MEETINGS

##### 3.1. MARKETING OBLIGATIONS

Both parties are committed to providing sustained Marketing support for the promotion of the Bed Mark (as hereinafter defined) through the Term of this Agreement. The parties agree to use reasonable business efforts to implement the Marketing activities as specifically described on Exhibit 3.1 attached hereto and made a part hereof.

##### 3.2. PERIODIC REVIEW MEETINGS

In an effort to keep both parties fully informed as to the status of any all aspects of this Agreement, and periodically throughout the year, representatives of Radisson and Select Comfort will meet and review the status of the program contemplated by this Agreement. Each such meeting will take Radisson's and Select Comfort's mutual objectives into account, and will be aimed at improving and re-evaluating the program if the parties deem it necessary. Additionally, the meetings will specifically address any warranty reports delivered pursuant to Section 6.2 hereof and the parties will endeavor to reasonably and mutually resolve any warranty issues in a fair and equitable manner. Full review meetings will take place on or about July 1, 2005, and July 1, 2006. Quarterly review meetings will take place every quarter beginning October 1, 2004, through the term of this Agreement.

#### ARTICLE 4 - PRODUCT FEATURES, JOINT TRADEMARK RIGHTS AND OTHER INTELLECTUAL PROPERTY RIGHTS

##### 4.1. PRODUCT FEATURES

The Beds will incorporate the features and will include the "tick" design specified on Exhibit 4.1 attached hereto and made a part hereof.

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During the Term, Select Comfort agrees that it will not offer the "tick" design specified on Exhibit 4.1 to any other party for any other purpose.

#### 4.2. JOINT TRADEMARK RIGHTS

The Beds manufactured, sold and marketed pursuant to this Agreement will be manufactured, marketed and sold under the trade name and the logo and design specified on Exhibit 4.2 attached hereto and made a part hereof (the "Bed Marks"). The Bed Marks will be jointly owned by the parties hereto and will be used solely and exclusively for the purposes specified in this Agreement. The parties agree to cooperate in connection with any registration of the Bed Marks in order to fully recognize and protect the joint ownership of the Bed Marks contemplated by this Agreement. Any use of the Bed Mark, other than as expressly permitted under this Agreement, shall be an infringement of the non-user's intellectual property rights. Notwithstanding the foregoing, each of the parties hereto will have the right to use any aspect of the Bed Marks that is currently used as, or as a part of, a trademark, trade name, service mark or similar mark owned and/or used by such party.

Nothing in this Agreement shall ever be construed as giving Select Comfort any right, title or interest in the Radisson Marks, or as giving Radisson any right, title or interest in the Select Comfort Marks, except to the extent that any such marks are incorporated in the Bed Marks, which may be used in accordance with this Agreement, and except for such use as may be consistent with the prior written approval of the owner of the respective marks for purposes of the Marketing efforts contemplated by this Agreement. Upon termination or expiration of this Agreement, all use of the Bed Marks shall cease and any other permitted use of the Radisson Marks by Select Comfort or the Select Comfort Marks by Radisson shall cease.

#### 4.3. OTHER INTELLECTUAL PROPERTY RIGHTS

Except for the Bed Marks to be jointly owned and limited to use in accordance with the terms of this Agreement and except for the Radisson Marks, which shall remain the sole and exclusive property of Radisson, all other intellectual property rights of any kind or description related to the Beds or their manufacture, marketing and sale, including without limitation any patents, patent applications, patentable features, designs or processes, trade secrets, trademarks, trade names, service marks or similar intellectual property rights of any kind or description shall remain the sole and exclusive property of Select Comfort.

### ARTICLE 5 - PRODUCT PRICING AND PRODUCT ORDERS

#### 5.1. PRODUCT PRICING

The pricing terms for the Beds are set forth in Exhibit 5.1 attached hereto and made a part hereof.

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#### 5.2. PRODUCT ORDERS

All orders for Beds will be placed by the Hotels through Guest Supply, Inc. If Guest Supply, Inc. fails to adequately coordinate such orders on behalf of the Hotels, Radisson may, in its sole discretion: (1) identify a suitable replacement (which shall be subject to Select Comfort's reasonable approval); or (2) assume responsibility for the Hotels' orders. Select Comfort will provide reasonable assistance to Guest

Supply in the development of order guidelines to be used by the Hotels when placing orders. All orders shall allow for a minimum of sixty (60) days from the date of order to the date of delivery. Select Comfort also agrees that orders of Beds for the Hotels under this program will be processed on a priority basis versus any other bed orders that Select Comfort may receive from the Hotel or Interval/Timeshare Industry.

### 5.3. PRODUCTION CAPACITY

Radisson acknowledges and agrees that all of the Beds are made to order and the pricing specified on Exhibit 5.1 is based on maximum monthly production volumes (the "Production Limits"). The Production Limits for 2004 are:

June	XXX Beds
July	XXX Beds
August	XXX Beds
September	XXX Beds
October	XXX Beds
November	XXX Beds
December	XXX Beds

The Production Limits in 2005 and 2006 are XXX Beds per month except for November, which shall be XXX Beds, and December, which shall be XXX Beds. If fewer Beds than the Production Limit are ordered in any month, any amount by which the order volume falls below the Production Limit shall not be carried forward or be added to the Production Limit in any subsequent month. Select Comfort shall not be obligated to produce or deliver more than one hundred and ten percent (110%) of the Production Limit in any month without its prior written consent, even if production or delivery of more than one hundred and ten percent (110%) of the Production Limit per month shall become necessary for the Hotels to meet the minimum Bed purchase requirements for Radisson to retain or extend the Exclusivity set forth in Section 2.2 hereof.

### 5.4. MORATORIUM ON DELIVERY AND INSTALLATION

Radisson acknowledges and agrees that Select Comfort shall not be obligated to deliver or install any Beds between November 15 of each year and January 1 of the following year without its prior written consent, even if delivery or installation of Beds during such period shall become necessary for the Hotels to meet the minimum Bed purchase

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requirements for Radisson to retain or extend the Exclusivity set forth in Section 2.2 hereof.

## ARTICLE 6 - INSTALLATION, TRAINING, CUSTOMER SERVICE AND WARRANTY

### 6.1. INSTALLATION AND TRAINING

Select Comfort will provide installation services, and training to Hotel staff on installation and maintenance, in connection with the first twenty-four (24) Beds installed at each Hotel for the "Total" price set forth on Exhibit 5.1. After installation of the first 24 Beds at a Hotel, the Hotel will have the option to purchase installation services for the price set forth on Exhibit 5.1 or to install the Beds at the Hotel's expense.

### 6.2. CUSTOMER SERVICE AND WARRANTY

Select Comfort will establish a toll-free Select Comfort

"Radisson-dedicated" customer service line for the benefit of both Hotel employees and guests. Select Comfort agrees to provide Radisson a monthly report summarizing calls received from Hotels, in order for the parties to proactively address common issues as they arise. Each Bed purchased by the Hotels during the Term of this Agreement will be covered by the warranty terms set forth on Exhibit 6.2 attached hereto and made a part hereof. Select Comfort also agrees to provide Radisson a monthly report summarizing all warranty-related "activity" by the Hotels, including specific Bed components replaced or repaired, and whether or not such activity was covered under the applicable warranty. Upon a sale of a Hotel with the Beds, or upon a Hotel leaving the Radisson System for any reason, the warranty will continue to be applicable for the remaining term of the warranty so long as the Beds remain in the Hotel.

## ARTICLE 7 - PRODUCT LIABILITY AND LEGAL REQUIREMENTS

### 7.1. PRODUCT LIABILITY

Select Comfort will indemnify, defend and hold harmless Radisson and its Affiliates against and from any claims for bodily injury or property damage caused by any defect in the design, materials or manufacturing of the Beds, or otherwise caused by any unreasonable risk or hazard presented by the Beds as used in the ordinary course and for the intended purposes ("Product Liability Claims"). While Product Liability Claims will ultimately not include any injury or damage caused by any abuse or misuse of the Beds not caused by Select Comfort or any injury or damage caused by the negligence or willful misconduct of Radisson, its Affiliates, the Hotels or the guests of the Hotels, Select Comfort upon notice by Radisson will be the "Indemnifying Party" as defined in Section 12.3 herein for any Product Liability Claim related to the Beds, unless it is reasonably apparent on the face of such claim that it is not a Product Liability Claim, or if not reasonably apparent, until such

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time as a court of competent jurisdiction determines that such a claim is not a Product Liability Claim.

### 7.2. SELECT COMFORT'S LEGAL RESPONSIBILITY

Select Comfort represents and warrants that each of the Beds sold and delivered hereunder, at the time of its sale and delivery, will be in full compliance with all Legal Requirements applicable to the sale and delivery of the Beds for the purposes intended by this Agreement, including flammability standards applicable to mattresses for commercial use in the country, state or province in which its Beds are installed. Select Comfort assumes no responsibility whatsoever for any Legal Requirements applicable to the ownership or operation of the hotel properties, including without limitation any applicable zoning, fire code or similar requirements of the jurisdictions in which the respective hotels are owned and operated.

### 7.3. RADISSON'S AND THE HOTEL'S LEGAL RESPONSIBILITY

The Hotels will be solely responsible for the operation of their respective hotel properties in full compliance with all Legal Requirements applicable to the ownership and operation of hotel properties, including all applicable zoning, fire code and other similar requirements of the jurisdictions in which the respective hotels are owned and operated. Radisson assumes no duty to review, inspect or approve the Beds with respect to compliance with any Legal Requirements. Radisson's inspections, reviews or approvals are solely for the purpose of determining compliance with its design standards and with respect to operational considerations, and presentation of the Radisson Marks.

Radisson's approval is not an assurance, representation or warranty: (i) that the Bed has been manufactured in accordance with Legal Requirements; or (ii) that all or any part of the Bed is safe, suitable, fit or proper for its intended use or purpose. This applies even though Radisson may have commented on any of these matters in connection with any inspections, reviews or approvals. Radisson is not responsible for compliance with, and Select Comfort must not rely on any information Radisson provides with respect to the applicability of or compliance with, any Legal Requirements regarding the manufacturing, selling, installation or operation of the Beds.

## ARTICLE 8 - OWNERSHIP OF CUSTOMER INFORMATION/DATABASES

### 8.1. OWNERSHIP OF CUSTOMER INFORMATION

Each party acknowledges that the other's proprietary databases are valuable assets of such other party's enterprise. As such, nothing in this Agreement will affect the ownership of information on customers that already exists in each party's databases currently, or which may be added in the future through other sources.

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## ARTICLE 9 - FORCE MAJEURE

### 9.1. DEFINITION OF FORCE MAJEURE

"Force Majeure" means any event or condition, not existing as of the date of signature of this Agreement, not reasonably foreseeable as of such date and not reasonably within the control of either party, which reasonably prevents in whole or in material part the performance by one of the parties of its obligations hereunder or which renders the performance of such obligations so difficult or costly as to make such performance commercially unreasonable. Without limiting the foregoing, the following will constitute events or conditions of Force Majeure: acts of State or governmental action (including specifically the failure of any government to grant any license, authorization or approval required for performance of this Agreement), riots, war, strikes, lockouts, prolonged shortage of energy supplies or utilities, epidemics, fire, flood, hurricane, typhoon, earthquake and explosion.

### 9.2. NOTICE

Upon giving notice to the other party, a party affected by an event of Force Majeure shall be released without any liability on its part from the performance of its obligations under this Agreement, except for the obligation to pay any amounts due and owing hereunder, but only to the extent and only for the period that its performance of such obligations is prevented by the event of Force Majeure. Such notice shall include a description of the nature of the event of Force Majeure, and its cause and possible consequences. The party claiming Force Majeure shall promptly notify the other party of the termination of such event. During the period the performance of one of the parties of its obligations under this Agreement has been suspended by reason of an event of Force Majeure, the other party may likewise suspend performance of all or part of its obligations, except for the obligation to pay amounts due and owing, to the extent commercially reasonable.

### 9.3. CONFIRMATION

The party invoking Force Majeure shall provide to the other party with written confirmation of the existence of the circumstances constituting Force Majeure. Such evidence may consist of a statement or certificate of an appropriate governmental department or agency where available, or

a statement describing in detail the facts claimed to constitute Force Majeure.

9.4. SUSPENSION OF PERFORMANCE

If an event of Force Majeure occurring at any time after the execution of this Agreement prevents performance hereunder by either party and continues for more than six (6) consecutive months, either party shall have the right to terminate this agreement on written notice to the other without any liability hereunder, except the obligation to make payments due to such date.

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ARTICLE 10 - TERMINATION

10.1. TERMINATION

This Agreement may be terminated prior to its ending date for the following:

A. By either party effective immediately upon notice to the other party in the event of the filing of a voluntary or involuntary bankruptcy petition by such other party, an assignment for the benefit of creditors by such other party, or the appointment of a receiver for such other party; or

B. By either party, if the other party is in material breach of its obligations contained in this Agreement, and such breach is not cured to the reasonable satisfaction of the non-breaching party within a period of thirty (30) days after written notice setting out the breach in reasonable detail. If the material breach is such that it cannot reasonably be cured within thirty (30) days, then the non-breaching party may not terminate this Agreement as long as the party in breach begins the cure within thirty (30) days and proceeds diligently and in good faith to accomplish the cure. If such breach is not cured to the reasonable satisfaction of the non-breaching party within ninety (90) days after the initial written notice, the Agreement may be terminated. Notwithstanding the foregoing, the failure of the Hotels to order, purchase and install sufficient quantities of the Beds in a timely manner as may be necessary to maintain or extend the Exclusivity under this Agreement shall not be a breach that is subject to cure under the foregoing provision.

ARTICLE 11 - INSURANCE

11.1. POLICY COVERAGE AND AMOUNT

At no cost to Radisson, during the term of this Agreement, Select Comfort will maintain commercial general liability insurance (with products and completed operations coverage) on an occurrence basis with combined single-limit coverage for personal and bodily injury and property damage of at least ten million dollars (\$10,000,000) per occurrence. The policies must also provide for the following:

A. "Radisson Hotels International, Inc. and its subsidiaries and its Affiliates" must be named as additional insureds; and

B. Radisson must receive 30 days' notice of any cancellation, non-renewal and material changes in the policy.

11.2. QUALIFICATIONS AND EVIDENCE

Select Comfort will obtain all policies with companies having a Best

Select Comfort will provide Radisson with certificates of insurance acceptable to Radisson evidencing that the policies are in effect within 30 days of the date of this Agreement, and at least 10 days prior to the expiration of any policy.

11.3. WAIVER OF SUBROGATION AND RELEASE

Wherever Radisson cannot be named as an additional insured under any insurance coverage required pursuant to this Agreement, Select Comfort will require the insurance company to include in the policy that the insurance company has no right of subrogation against Radisson or their respective Affiliates.

The required policies are for Select Comfort's, Radisson's and its Affiliates' benefit and protection. Radisson makes no warranty or representation that the policies are adequate for Select Comfort's needs whatsoever. The insurance coverage required to be obtained by Select Comfort is the primary coverage Select Comfort's obligation to maintain the required insurance is not limited in any way because of any insurance that Radisson or its Affiliates carries. Neither Select Comfort nor any of its insurance providers will deny coverage of any losses, whether by Select Comfort, Radisson or its Affiliates because of any insurance that Radisson or its Affiliates carry, and Select Comfort has no right to any additional coverage obtained by Radisson or its Affiliates.

ARTICLE 12 - INDEMNIFICATION; ATTORNEYS' FEES

12.1. INDEMNIFICATION BY SELECT COMFORT

Select Comfort agrees to indemnify and hold harmless Radisson and its Affiliates against and from, all Payments due to any Claim, brought by or on behalf of any Third Party or otherwise, with respect to:

- A. Any breach by Select Comfort of its obligations under this Agreement; or
- B. Any misrepresentation or breach of warranty by Select Comfort under this Agreement; or
- C. Any Product Liability Claim.

Select Comfort's obligations under this Section 12.1 do not apply to any Claim that is directly caused by Radisson's or any of its Affiliates negligence or willful misconduct. For purposes of this Article, Radisson and its Affiliates includes their respective officers, directors, shareholders, managers, members, governors, employees, agents, Third Party contractors, successors and assigns.

12.2. INDEMNIFICATION BY RADISSON

Radisson agrees to indemnify and hold harmless Select Comfort and its Affiliates against and from, all Payments due to any Claim, brought by or on behalf of any Third Party or other wise, with respect to:

- A. Any breach by Radisson of its obligations under this Agreement; or
- B. Any misrepresentation or breach of warranty by Radisson under this

Agreement; or

C. Any claim asserted by any owner or operator of a Hotel in the Radisson System under any franchise or similar agreement between Radisson and any other party or under any applicable franchise, business opportunity or similar law or provision.

Radisson's obligations under this Section 12.2 do not apply to any Claim that is directly caused by Select Comfort's or any of its Affiliates negligence or willful misconduct. For purposes of this Article, Select Comfort and its Affiliates includes their respective officers, directors, shareholders, managers, members, governors, employees, agents, Third Party contractors, successors and assigns.

#### 12.3. NOTICE AND OPPORTUNITY TO DEFEND

In the event that any party shall become entitled to indemnification under this Agreement, whether due to the assertion of a claim by any third party or otherwise, the party entitled to indemnification hereunder (the "Indemnified Party") shall promptly notify the party responsible to provide indemnification hereunder (the "Indemnifying Party") specifying in reasonable detail the facts underlying the claim for indemnification. The Indemnifying Party shall not be relieved of its responsibility to provide indemnification under this Agreement due to any failure of the Indemnified Party to provide timely notice of a claim for indemnification hereunder unless the delay in providing such notice shall have materially compromised the Indemnifying Party's ability to fully and adequately defend the claim.

Within ten (10) business days following the receipt of a claim for indemnification from any Indemnified Party hereunder, the Indemnifying Party shall notify the Indemnified Party as to whether the Indemnifying Party will assume the defense of any third party claim underlying the claim for indemnification hereunder. In the event that the Indemnifying Party assumes the defense of the claim, the Indemnifying Party shall be entitled to fully control the defense of the claim and to settle, negotiate or compromise the claim, so long as any such settlement or compromise does not result in any injunctive or similar non-monetary judgment against the Indemnified Party that has any ongoing effect and so long as the Indemnified Party is fully indemnified against any monetary judgment arising from such claim. Upon notice thereof to the Indemnifying Party, the Indemnified Party shall be entitled, at the expense of the Indemnified Party, to monitor and participate in the defense of the indemnified claim, subject to the control of the Indemnifying Party.

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#### 12.4. SURVIVAL

The indemnification and other obligations contained in this Article will continue in full force and effect subsequent to and notwithstanding the expiration or termination of this Agreement.

### ARTICLE 13 - INJUNCTIVE RELIEF

#### 13.1. AVAILABILITY OF INJUNCTIVE RELIEF

A breach of this Agreement by either Select Comfort or Radisson relating to any of the matters set out below may cause irreparable harm to Radisson or Select Comfort, as the case may be, for which monetary damages may be an inadequate remedy. Therefore, in such event, in addition to any other remedies Radisson or Select Comfort may have under this Agreement or at law or in equity, Radisson or Select Comfort may seek and obtain the entry of temporary or permanent injunctions and

orders of specific performance enforcing the provisions of this Agreement with respect to: (i) the Radisson Marks, the Select Comfort Marks or the Bed Mark; (ii) the System; (iii) the obligations of Select Comfort or Radisson, as the case may be, upon termination or expiration of this Agreement; (iv) the unauthorized disclosure or threatened disclosure of proprietary or confidential information of either party; or (v) any act or omission by either party or either party's employees that: (a) constitutes a violation of any Legal Requirement; or (b) may impair the good will associated with the Radisson Marks, the Select Comfort Marks, the Bed Marks or the business enterprise of either of the parties hereto.

13.2. NO NECESSITY FOR POSTING OF BOND

Unless required by the court granting any such injunctive relief, neither party shall be required to post a bond or other security with respect to obtaining injunctive relief under this Agreement.

ARTICLE 14 - CONFIDENTIALITY

14.1. CONFIDENTIALITY

The parties agree that (i) the specific terms of this Agreement, (ii) all information as to source, quantity, and price of goods and services, and (iii) all information regarding either party's products, business, customers, or methods of operation learned during the term of this Agreement or in anticipation of entering into this Agreement shall be maintained in confidence and not be released to any third party for any reason whatsoever other than: (i) pursuant to a validly issued subpoena from a court or governmental authority having jurisdiction over the party or pursuant to a discovery request made under the Federal Rules of Civil or Criminal Procedure or similar state court rules and to which the party is required to respond or as may be required to implement the terms of this Agreement; or (ii) as may be required by applicable rules of the Securities and Exchange Commission (the "SEC") as reasonably

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determined by counsel to any party hereto with a class of securities registered under the Securities Exchange Act of 1934, subject, in each case, to reasonable notification to the other party prior to release of such information, in order to allow the other party an opportunity to oppose such court action or governmental authority or to participate in the process to seek confidential treatment of any information otherwise required to be filed under applicable SEC rules. All confidential and proprietary information, which the parties have obtained from each other shall be returned upon the expiration or earlier termination of this Agreement. The provisions of this paragraph shall survive the expiration or earlier termination of this Agreement.

ARTICLE 15 - MISCELLANEOUS

15.1. SEVERABILITY

All provisions of this Agreement are severable. If pursuant to the decision of any court having jurisdiction, any provisions, in whole or in part are not enforceable, the remainder of this Agreement will continue to be in full force and effect, and the applicable parts of the affected provisions are superceded and modified by such applicable law. If either party can establish that such modifications would constitute a material deviation from the general purpose and intent of this Agreement, either party may terminate this Agreement on not less than thirty (30) days' notice. A valid termination pursuant to this Section is without liability by either party to the other party except for any



causes of action a party has against the other for matters occurring up to and through the date of such termination.

15.2. WAIVER

The failure, refusal or neglect of one party to require the other party to comply with any provision of this Agreement, in whole or in part, does not constitute a waiver by the former of its right to require full compliance with the same or different provisions in the future, regardless of the acceptance of payments or performance by the party seeking compliance.

15.3. GOVERNING LAW

The interpretation, validity and enforcement of this Agreement and the relationship between the parties is subject to and governed by the laws (statutory or otherwise) of the State of Minnesota without regard to its conflicts of laws provisions.

15.4. VENUE AND JURISDICTION

All Claims whatsoever, arising out of or related to this Agreement in any way, must be commenced, filed and litigated before a court of competent jurisdiction located in Hennepin County, Minnesota. Both parties submit to personal jurisdiction of the State and Federal courts in such county for such purpose.

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15.5. JURY WAIVER

Each party knowingly and voluntarily waives the right to a trial by jury in any litigation arising under, as a result of or in connection with this Agreement or any franchise or business opportunity laws.

15.6. CLAIMS

Except for those Claims that are brought pursuant to the indemnification or insurance coverage required under Articles 10 and 11 hereof, upon expiration or termination of this Agreement, neither party will commence any cause of action related to or arising out of this Agreement, unless commenced within one year following the effective date of expiration or termination.

15.7. ENTIRE AGREEMENT

This Agreement, including the exhibits attached hereto and made a part hereof and any amendments hereto that are validly executed and delivered by each of the parties hereto, collectively constitutes the entire agreement between the parties with respect to the subject matter hereof, and this Agreement supersedes and terminates all prior agreements or understandings, either oral or in writing, between the parties hereto. Any representations, warranties, inducements, promises, understandings or agreements between the parties, which are not in writing and signed by the parties, are void and not enforceable.

15.8. MODIFICATIONS

Oral modifications to this Agreement, including those by way of release, amendment, waiver or otherwise, are not valid or enforceable. The parties may modify this Agreement only by a written agreement signed by a duly authorized representative of each party.

15.9. HEADINGS

The headings of the Articles and Sections of this Agreement are for

convenience of reference only and do not define, limit or construe their contents.

15.10. NOTICES

Any notices required or permitted under this Agreement must be in writing and must be delivered either personally, by fax, by Certified United States Mail or by reliable expedited delivery companies including Federal Express, Airborne Express and DHL. Notices by fax are deemed delivered and received upon transmission with a confirmation of such transmission. Notices by Certified United States Mail are deemed delivered and received on the second business day immediately following the day on which the notice was given to the United States Postal Service. Notices by expedited delivery are deemed delivered and received on the business day immediately following the day on which the notice was given to the expedited delivery company. Information for notices is

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as indicated in the first paragraph of this Agreement.

15.11. EXECUTION/COUNTERPARTS

The parties may sign more than one identical copy of this Agreement, each of which is an original. When parties sign different, but identical copies of this Agreement, the copies constitute one Agreement.

15.12. ATTORNEYS' FEES

All reasonable and necessary costs and expenses, including attorneys' fees, incurred by Radisson or Select Comfort in enforcing any provisions of this Agreement, or in asserting or defending against any Claims brought by one party against the other party under this Agreement, whether through injunctive relief or otherwise, will be paid by the non-prevailing party to the prevailing party in such action.

15.13. ACTIONS BY OTHERS

Where either party to this Agreement is prohibited by this Agreement from directly taking any action, or where action by either party to this Agreement would constitute a default, such party agrees that it will not encourage, authorize or permit any other Person, directly or indirectly or under its direct or indirect control to take such action.

15.14. PERFORMANCE THROUGH OTHERS

Either of the parties hereto may perform any or all of its obligations under this Agreement directly or through one or more of its wholly owned subsidiaries, provided however, that the assignment to or performance of any such obligations by any such subsidiary corporation will not relieve any party hereto of any of its primary responsibility under this Agreement. If any such obligations are performed by any such subsidiary corporation, the right to such performance will still run directly to the other party to this Agreement.

15.15. SURVIVAL

The provisions of Articles 7, 8, 12, 13, 14 and 15 hereof, and of Sections 4.2 and 4.3 hereof, shall survive the termination of this Agreement and will continue to govern the rights and obligations of the parties hereto indefinitely following the termination of this Agreement.

15.16. COMPLIANCE WITH LAWS

Notwithstanding any provision to the contrary, each party's performance is subject to, and each party will comply with, all Legal Requirements,

including those of all countries in which either party conducts business that prohibits unfair, fraudulent or corrupt business practices such as those that are comparable to the United States Foreign Corrupt Practices

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Act and the International Money Laundering Abatement and Anti-Terrorist Financing Act, otherwise known as the Patriot Act.

15.17. TIME OF THE ESSENCE

Time is of the essence in the performance of every provision of this Agreement.

15.18. THIRD PARTY BENEFICIARIES

This Agreement is for the sole benefit of the parties and is not for the benefit of any Third Parties.

15.19. CUMULATIVE RIGHTS

The remedies provided for in this Agreement are not exclusive. Either party is free to pursue such other remedies as may be available at law or in equity.

15.20. USE OF DEFINITIONS/TERMS

The use of another tense of the defined term, or its use as a noun, adjective or adverb, or otherwise, means the same as the defined term, modified by the context of the sentence in which it is used. All personal pronouns, whether used in the masculine, feminine or neuter gender, include all genders; the singular includes the plural and the plural includes the singular.

15.21. COPIES

Photocopies and facsimiles of a signed original of this Agreement are fully binding and effective as originals.

15.22. INTERNAL POLICIES

Each party's internal policies and procedures, whether or not communicated to the other party, are intended for such first party's use only, are not binding on such first party with respect to its relationship with the other party, and are not a part of or an amendment to this Agreement.

15.23. EXHIBITS

All exhibits attached to this Agreement are a part of it and fully incorporated into it.

15.24. INTERPRETATION

Neither this Agreement nor any of its provisions is to be construed against or interpreted to the disadvantage of either party because a party drafted this Agreement or the provision.

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15.25. INDEPENDENT CONTRACTOR

Radisson and Select Comfort are each independent contractors. This Agreement does not create any relationship of joint venturers, partners, agents, servants, employees, fiduciaries or representatives of each

other.

15.26. DEFINITIONS.

The following definitions shall be used for purposes of this Agreement.

AFFILIATE. Any Person Controlled by, Controlling or under common Control with either party.

CLAIM. Any claim, challenge, demand, cause of action, lawsuit, dispute, controversy, investigation or administrative proceeding.

CONTROL. The right or ability, directly or indirectly, to cause a Person to act in accordance with another Person's instructions.

EXCEPTIONAL CATEGORY. Four Seasons Hotels and Resorts, The Ritz Carlton, St. Regis Hotels and Resorts, Intercontinental Hotels and Resorts, and Mandarin Oriental. Additions and deletions to this list are only as mutually agreed by the parties hereto

GOVERNMENTAL AUTHORITY. Any governmental entity, and any political or other subdivision of any governmental entity, and any agency, department, commission, board, bureau, court or instrumentality of any of them, which, at any time, has competent jurisdiction over aspect of this Agreement.

HOTEL. A Radisson hotel operated in the United States, Canada or the Caribbean using the System pursuant to a written agreement with Radisson.

LEGAL REQUIREMENTS. Any law, code, ordinance, order, decision, rule or regulation of any Governmental Authority.

MARKETING. All activities related to marketing, sales, advertising, promotion and public relations with respect to the Hotels, the System, and the Beds pursuant to this Agreement, as more specifically identified on Exhibit 3.1 attached hereto and made a part hereof.

PAYMENTS. All payments of money, including those with respect to fines, penalties, taxes, losses, damages, costs and expenses, such as reasonable attorney fees, investigation expenses, court costs, deposition expenses, and travel and living expenses.

PERSON. Any natural person or legal entity, including trustees, representatives, administrators, heirs, executors, partnerships, corporations, limited liability companies, trusts, unincorporated organizations and governmental agencies, departments and branches.

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PURCHASE. Transmission of the property rights to the Beds from Select Comfort to the Hotels via sale, discount, negotiation, pledge, lien, issue or re-issue, or any other voluntary transaction creating an interest in the Beds, including contracts to purchase. In any event, the term "purchase" shall mean that the purchaser shall have fully paid for and taken delivery of the purchased goods.

RADISSON MARKS. The name Radisson(R) and the signature logo Radisson(R) with the brush stroke used in conformance with Radisson's business system, and all other trademarks, service marks, trade names, copyrights, insignia, emblems, slogans, logos, commercial symbols, signs, trade dress (including interior and exterior building designs and specifications and the motif, decor, and color combinations), and all other visual identification, by which the Hotels are identified and publicized, including the good will associated with all of them.

SELECT COMFORT MARKS. The trademarks Select Comfort(R) and Sleep Number(R) and all other trademarks, service marks, trade names, copyrights, insignia, emblems, slogans, logos, commercial symbols, signs, trade dress by which Select Comfort beds are identified and publicized, including the good will associated with all of them.

SYSTEM. The Radisson Marks, and other distinctive elements developed and owned by, or made available by its Affiliates to, Radisson, and the systems made available to Radisson for the construction and operation of the Hotels and other hotels authorized to use the System, including all good will.

SYSTEM STANDARD. Any element of the System that the Hotels are required to implement pursuant to the terms of any applicable franchise or similar agreement in place between Radisson and the Hotel owners and operators.

THIRD PARTY. Any Person, other than Radisson, Select Comfort and their respective Affiliates.

Executed as of the date set forth at the beginning of this Agreement.

RADISSON HOTELS INTERNATIONAL. INC.

SELECT COMFORT CORPORATION

By: /s/Bjorn Gullakson  
-----  
Name: Bjorn Gullakson  
-----  
Its: Executive Vice President  
-----

By: /s/Keith C. Spurgeon  
-----  
Name: Keith C. Spurgeon  
-----  
Its: Senior VP - Sales  
-----

EXHIBIT INDEX

EXHIBIT	DESCRIPTION
2.2A	List of Hotels to which Select Comfort has previously sold beds
3.1	Marketing Plan
4.1	The Products and Models
4.2	The Bed Mark and Logo
5.1	Product Pricing
6.2	Warranty Terms

EXHIBIT 2.2A

List of Hotels Select Comfort has previously sold beds

XXX

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

EXHIBIT 3.1

Liberty Marketing Budget & Spending Recommendations  
5/18/2004

1 - Budget

<TABLE>

<S>	<C>	<C>	<C>	<C>
A - Funds from sale of beds to Radisson	2004 ----	2005 ----	2006 ----	2007 ----
(Projections)				
Fund/bed = XXX	\$XXX	\$XX	\$XXX	\$XXX
Annual volume (low qty)=	XXX	XXX	XXX	XXX
Annual Budget =	\$XXX	\$XXX	\$XXX	\$XXX
Fund/bed = XXX	\$XXX	\$XXX	\$XXX	\$XXX
Annual volume (high qty)=	XXX	XXX	XXX	XXX
Annual Budget =	\$XXX	\$XXX	\$XXX	\$XXX
B - Trial:Conversions (Projections)	2004 ----	2005 ----	2006 ----	2007 ----

Based on forecasts previously provided. If conversion is higher

more spending will occur; If conversion is lower less spending will occur.

Units from Trial;Conversion	XXX	XXX	XXX	XXX
ASP = XXX	\$XXX	\$XXX	\$XXX	\$XXX
Media %/Sales = XXX% (same as SC Corporate rate)	XXX%	XXX%	XXX%	XXX%
Annual Forecasted budget =	\$XXX	\$XXX	\$XXX	\$XXX
Total Budget Potential				
Lower Qtys	\$XXX	\$XXX	\$XXX	\$XXX
Higher Qtys	\$XXX	\$XXX	\$XXX	\$XXX

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

2 - Funding Split Recommendations - Select Comfort:Radisson

<S>	<C>	<C>	<C>	<C>
	2004	2005	2006	2007
	----	----	----	----

A - Funds from sale of beds to Radisson

Lower Qtys				
Select Comfort	%	XXX%	XXX%	XXX%
	\$	\$XXX	\$XXX	\$XXX
Radisson				
	%	XXX%	XXX%	XXX%
	\$	\$XXX	\$XXX	\$XXX
Higher Qtys				
Select Comfort	%	XXX%	XXX%	XXX%
	\$	\$XXX	\$XXX	\$XXX
Radisson				
	%	XXX%	XXX%	XXX%
	\$	\$XXX	\$XXX	\$XXX

B - Trial:Conversions

Select Comfort				
	%	XXX%	XXX%	XXX%
	\$	\$XXX	\$XXX	\$XXX
Radisson				
	%	XXX%	XXX%	XXX%
	\$	\$XXX	\$XXX	\$XXX

<FN>

- Notes:
- 1 - Select Comfort requires, at minimum, the % splits above to deliver consumer impressions at the level being communicated to franchisees for 2004 & 2005. WITH THESE SPLITS 2006 MARKETING ACTIVITIES/SUPPORT WOULD HAVE TO BE CHANGED AS FOLLOWS: RADIO/PRINT/TV FLIGHTS WOULD HAVE TO BE REDUCED FROM 26 WEEKS TO 14-15 WEEKS (REFLECTED ON ATTACHED FLOW CHART).
  - 2 - Select Comfort agrees to the following media support and tests at the following room penetration levels (assuming consistent with agreed upon media objectives):
    - Radio/Print = XXX%
    - TV = XXX%
    - Tests (Print, Inquiries) = XXX%
  - 3 - All funds committed to be spent within 6 months of "acknowledgement of funds"
  - 4 - Select Comfort and Radisson will review marketing budgets and

spending assumptions annually.

</FN>  
</TABLE>

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

2004 - 2008 PROJECT LIBERTY SPENDING ESTIMATES

<S> TACTIC	<C> FY 2004	<C> Q4 2004 ESTIMATE	<C> FY 2005 XXX%	<C> FY 2006 XXX%	<C> FY 2007 XXX%	<C> FY 2008 XXX%
Promotions	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Print	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Television	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Ad Production	\$ XXX					
	-----					
	\$ XXX	\$ XXX	\$ XX	\$ XXX	\$ XXX	\$ XXX
Online Advertising, Keywords	\$ XXX	\$ XXX				
E-Partnerships, IATA Project	\$ XXX					
	-----					
	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
AAA Tourbooks, Atlas	\$ XXX					
AARP	\$ XXX					
	-----					
	\$ XXX		\$ XXX	\$ XXX	\$ XXX	\$ XXX
Directory of Accommodations	\$ XXX		\$ XXX	\$ XXX	\$ XXX	\$ XXX
Sponsorships	\$ XXX					
Research (Benchmark, Other)	\$ XXX		*	*	*	*
Research (Web)	\$ XXX					
	-----					
	\$ XXX					
Other (website, Genuine Article, comment cards, meetings, misc.)	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Public Relations	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Direct Mail, Email	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
	-----					
SUBTOTAL	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
	=====					
Existing Partner Matching Funds	\$ XXX	\$ XXX				
Brand Differentiator Seed Money	\$ XXX	\$ XXX				
	-----					
TOTAL	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
	=====					

<FN>  
\*Funding from surplus and/or advertising development  
</FN>  
</TABLE>

(Table with media values and impression estimates excluded pursuant to request for confidential treatment and has been filed separately with the Commission.)



#### EXHIBIT 4.1

##### The Products and Models

The Sleep Number Bed for Radisson will incorporate these core features:

- o Adjustable Air-Chamber technology
- o Dual -Adjustability (Kings, Queens, Doubles)
- o Lightweight Construction
- o Hypoallergenic Materials
- o Modular Design
- o Corner Lock(TM)system for crisp, clean corners
- o Gussetted Pillowtop
- o 12 1/2" tall mattress
- o Exclusive Radisson/Sleep Number designed ticking material (made out of a Poly blend Belgian Damask cover)
- o Ticking with appropriate treatment to meet requirements specified below
- o Sleep Number firmness control system - with a single tethered, dual controller - to adjust each side independently. (Full size bed would have a single, larger chamber)
- o Non-slip material added to the underside of the mattress
- o Hospitality hose kit - to allow easier change out of pumps in guest rooms
- o Wood foundation with these features
  - Unique I-beam construction
  - Solid platform with rigid base
  - Covered with treated tick
  - Tested through 200,000 use cycle

The Sleep Number Bed for Radisson will be offered in 3 sizes - Eastern King (76" x 80"), Queen (60" x 80"), and Full/Double XL (54" x 80"). Note the Full/Double XL size will not be available to ship until January, 2005 after receiving input of whether this bed requires a single or double chamber.

The Sleep Number Bed for Radisson will incorporate flame retardant features as specified. The beds will meet the following test standards (A) for 2004 and (B) for 2005 and beyond:

- (A) NFPV #701; MVS #301; alternate to 16 CFR part 1632 Class B
- (B) NFPV #701; MVS #301; alternate to 16 CFR part 1632 Class B plus new California consumer requirements going into effect January, 2005

#### EXHIBIT 4.2

(partnership logo omitted)

##### THE PARTNERSHIP LOGO

The logo represents the unique partnership between Radisson Hotels & Resorts[R] and Select Comfort (The Sleep Number[R] bed). It is a fusion of the strengths of two national brands that at once establishes the identity of our new initiative, and at the same time allows the integrity of each individual brand to remain intact.

(partnership logo omitted)

The mark consists of the Radisson logo joined to a modified Sleep Number[R] bed logo by an extended green loop which emanates from the Radisson brush stroke. The configuration seen here is the only approved treatment of this new identity. Do not attempt to recreate this mark. Use only the provided artwork.

(partnership logo omitted)

COLORS

Being that this logo consists of two corporate identities, it is vital that the colors used in this mark are consistent with the prescribed colors of the two brands. The Radisson portion of the logo is Black (in the typography) and the Radisson green in the brush stroke/oval outline.

FOUR-COLOR RADISSON GREEN.  
35% Cyan and 100% Yellow.

SPOT-COLOR RADISSON GREEN.  
MSP-78553 K/7K9 Coated  
MSP-78651 K/7K9 Uncoated

PMS 382.

The Sleep Number[R] bed portion is to be rendered in Sleep Number[R] blue. With the exception of black & white usage, these are the only acceptable colors used.

FOUR-COLOR SLEEP NUMBER[R] BLUE.  
80 Cyan, 50% Magenta, 15% Yellow and 0% Black.

SPOT-COLOR SLEEP NUMBER[R] BLUE.  
PMS 653.

THE LOGO - USAGE/SAFE AREA

The combination of identities contained in this logo need to be protected from any outside graphic intrusions. We have established a boundary around the logo to preserve its integrity and to ensure that its impact will not be diminished by any extraneous imagery. The specified proportions are 15.0 units horizontally to 9.0 units vertically. Please keep all other visual elements clear of the safe area.

(partnership logo omitted)

THE LOGO - BLACK AND WHITE

The preferred printed version of this logo is four-color process. If printing in one color, black is the preferred color. Below are examples of black and white renderings.

(partnership logo omitted)

EXHIBIT 5.1

Final Project Liberty Pricing  
5/17/2004

<TABLE>

<S>	<C>	<C>
Size	Component	Price
Eastern King -----	Bed Set (Mattress & Foundation) (1)	\$ XXX
	Installation (2)	\$ XXX

	Freight (3)	\$	XXX
	Total	\$	XXX
Queen -----	Bed Set (Mattress & Foundation) (1)	\$	XXX
	Installation (2)	\$	XXX
	Freight (3)	\$	XXX
	Total	\$	XXX
Full (Single Chamber) -----	Bed Set (Mattress & Foundation) (1)	\$	XXX
	Installation (2)	\$	XXX
	Freight (3)	\$	XXX
	Total	\$	XXX

<FN>

- Notes: (1) Including component costs required to meet higher CA consumer flammability requirements
- (2) Installation - Once 24 beds per property have been installed & training delivered to Radisson employees than this becomes an option.
- (3) Freight - Based on FTL qtys. Actual cost will vary based on qty ordered as follows:

FTL (72 beds) \$XXX/bed  
 3/4 Truck (54 - 71 beds) \$XXX/bed  
 1/2 Truck (36 - 53 beds) \$XXX/bed  
 1/4 Truck (18 - 35 beds) \$XXX/bed  
 LTL (1 - 17 beds) \$XXX/bed

- (4) Double Bed (Dual Chamber) - Price is \$XXX (before installation and delivery)
- (5) For years 2006, 2007, 2008 Pricing will be adjusted as follows:

No more than XXX% increase annually

Cost increases justified basis market increases in key components as a % of bed cost:

Petroleum = XXX%  
 Labor & Overhead = XXX%  
 Rubber = XXX%  
 Wood = XXX%  
 Cotton/Fabric = XXX%  
 Other = XXX%

Price reviewed annually with Radisson prior to July 1st

</FN>  
 </TABLE>

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

EXHIBIT 6.2

WARRANTY PROGRAM

SLEEP NUMBER BED - MADE EXCLUSIVELY FOR RADISSON

PUMP (INCLUDING CONTROL), CHAMBER & FOAM COMPONENTS

-----  
Warranty - 15 Year Prorated Warranty

Warranty 100% - 4 years

Free From Defects in Materials & Workmanship

Normal "Wear & Tear" Not Covered

11 years prorated: Pump, Chamber & Foam Components

<TABLE>

<S>	<C> Max % Increase	<C> Price
PUMP	-----	-----
*Years 1-4 =	NA	Covered at 100%
**Year 5 =	NA	\$ XXX
Year 6 =	6%	\$ XXX
Year 7 =	6%	\$ XXX
Year 8 =	6%	\$ XXX
Year 9 =	6%	\$ XXX
Year 10 =	6%	\$ XXX
Year 11 =	6%	\$ XXX
Year 12 =	6%	\$ XXX
Years 13 - 15 =		\$ XXX

</TABLE>

<TABLE>

CHAMBER	Max % Increase	Price (for one chamber)			
<S>	<C>	<C>	<C>	<C>	<C>
		KING	QUEEN	FULL XL (SINGLE CHAMBER)	DOUBLE XL
*Years 1-4 =	NA	Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%
**Year 5 =	NA	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 6 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 7 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 8 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 9 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 10 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 11 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 12 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Years 13 - 15 =		\$ XXX	\$ XXX	\$ XXX	\$ XXX

</TABLE>

<TABLE>

Foam Components	Max % Increase	Price (for one chamber)			
<S>	<C>	<C>	<C>	<C>	<C>
		KING	QUEEN	FULL XL (SINGLE CHAMBER)	DOUBLE XL
SIDEWALLS					
*Years 1-4 =	NA	Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%
**Year 5 =	NA	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 6 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 7 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 8 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 9 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 10 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 11 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 12 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Years 13 - 15 =		\$ XXX	\$ XXX	\$ XXX	\$ XXX

</TABLE>

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

<TABLE>						
ENDWALLS	Max % Increase	Price (for one chamber)				
	-----	-----				
<S>	<C>	<C>	<C>	<C>	<C>	<C>
		KING	QUEEN	FULL XL (SINGLE CHAMBER)	DOUBLE XL	
		Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%	
*Years 1-4 =	NA					
**Year 5 =	NA	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 6 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 7 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 8 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 9 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 10 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 11 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 12 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Years 13 - 15 =		\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX

<TABLE>						
BASEPAD	Max % Increase	Price (for one chamber)				
	-----	-----				
<S>	<C>	<C>	<C>	<C>	<C>	<C>
		KING	QUEEN	FULL XL (SINGLE CHAMBER)	DOUBLE XL	
		Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%	
*Years 1-4 =	NA					
**Year 5 =	NA	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 6 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 7 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 8 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 9 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 10 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 11 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 12 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Years 13 - 15 =		\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX

<TABLE>						
CENTERWALL	Max % Increase	Price (for one chamber)				
	-----	-----				
<S>	<C>	<C>	<C>	<C>	<C>	<C>
		KING	QUEEN	FULL XL (SINGLE CHAMBER)	DOUBLE XL	
		Covered at 100%	Covered at 100%	NA	Covered at 100%	
*Years 1-4 =	NA					
**Year 5 =	NA	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Year 6 =	6%	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Year 7 =	6%	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Year 8 =	6%	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Year 9 =	6%	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Year 10 =	6%	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Year 11 =	6%	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Year 12 =	6%	\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX
Years 13 - 15 =		\$ XXX	\$ XXX	NA	\$ XXX	\$ XXX

<TABLE>						
	Max % Increase	Price (for one chamber)				
	-----	-----				

TOPPERPAD	Increase -----	chamber)				
<S>	<C>	<C>	<C>	<C>	<C>	<C>
		KING	QUEEN	FULL XL (SINGLE	CHAMBER)	DOUBLE XL
		Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%
*Years 1-4 =	NA					
**Year 5 =	NA	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 6 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 7 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 8 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 9 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 10 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 11 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 12 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Years 13 - 15 =		\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX

<FN>  
 \* Select Comfort pays freight back to property on 100% coverage warranty parts  
 \*\* Customer will return Pumps & Chambers upon Select Comfort's request to use in product analysis. Select Comfort will pay freight on these types of returns.  
 </FN>  
 </TABLE>

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

PILLOWTOP COVER:  
 Warranty - 180 Days 100%  
 Free From Defects in Materials & Workmanship  
 Normal "Wear & Tear" Not Covered  
 <TABLE>

Cover	Max % Increase -----	Price -----				
<S>	<C>	<C>	<C>	<C>	<C>	<C>
		KING	QUEEN	FULL XL (SINGLE	CHAMBER)	DOUBLE XL
		Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%	Covered at 100%
*Days 1-180	NA					
***Year 5 =	NA	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 6 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 7 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 8 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 9 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 10 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 11 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Year 12 =	6%	\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX
Years 13 - 15 =		\$ XXX	\$ XXX	\$ XXX	\$ XXX	\$ XXX

<FN>  
 \*Select Comfort pays freight on cover back to property for first 180 days.  
 \*\*After 180 days customer does not have to return covers to Select Comfort.  
 \*\*\*Property may purchase a cover at anytime through year 5 at \$XXX/XXX/XXX (King/Queen/Full XL/Double XL) per cover Note: Cover includes pillowtop cover and entire mattress casing  
 </FN>  
 </TABLE>

FOUNDATION:  
 Warranty - 10 Years 100%  
 Free From Defects in Materials & Workmanship  
 Normal "Wear & Tear" Not Covered  
 Customer pays freight both ways on foundations.

XXX = Confidential portion has been omitted pursuant to a request for confidential treatment and has been filed separately with the Commission.

SELECT COMFORT CORPORATION  
2004 STOCK INCENTIVE PLAN

1. PURPOSE OF PLAN.

The purpose of the Select Comfort Corporation 2004 Stock Incentive Plan (the "Plan") is to advance the interests of Select Comfort Corporation (the "Company") and its shareholders by enabling the Company and its Subsidiaries to attract and retain qualified individuals through opportunities for equity participation in the Company, and to reward those individuals who contribute to the achievement of the Company' objectives.

2. DEFINITIONS.

The following terms will have the meanings set forth below, unless the context clearly otherwise requires:

2.1 "BOARD" means the Board of Directors of the Company.

2.2 "BROKER EXERCISE NOTICE" means a written notice pursuant to which a Participant, upon exercise of an Option, irrevocably instructs a broker or dealer to sell a sufficient number of shares or loan a sufficient amount of money to pay all or a portion of the exercise price of the Option and/or any related withholding tax obligations and remit such sums to the Company and directs the Company to deliver stock certificates to be issued upon such exercise directly to such broker or dealer or their nominee.

2.3 "CAUSE" means (i) dishonesty, fraud, misrepresentation, embezzlement or deliberate injury or attempted injury, in each case related to the Company or any Subsidiary, (ii) any unlawful or criminal activity of a serious nature, (iii) any intentional and deliberate breach of a duty or duties that, individually or in the aggregate, are material in relation to the Participant's overall duties, or (iv) any material breach of any employment, service, confidentiality or non-compete agreement entered into with the Company or any Subsidiary.

2.4 "CHANGE IN CONTROL" means an event described in Section 12.1 of the Plan.

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

2.6 "COMMITTEE" means the group of individuals administering the Plan, as provided in Section 3 of the Plan.

2.7 "COMMON STOCK" means the common stock of the Company, par value \$0.01 per share, or the number and kind of shares of stock or other securities into which such Common Stock may be changed in accordance with Section 4.3 of the Plan.



2.8 "DISABILITY" means the disability of the Participant such as would entitle the Participant to receive disability income benefits pursuant to the long-term disability plan of the Company or Subsidiary then covering the Participant or, if no such plan exists or is applicable to the Participant, the permanent and total disability of the Participant within the meaning of Section 22(e)(3) of the Code.

2.9 "EFFECTIVE DATE" means May 20, 2004 or such later date as the Plan is initially approved by the Company's shareholders.

2.10 "ELIGIBLE RECIPIENTS" means all employees (including, without limitation, officers and directors who are also employees) of the Company or any Subsidiary and any non-employee directors, consultants and independent contractors of the Company or any Subsidiary. Non-employee directors shall only be eligible to participate through the limited, automatic grant provisions specified in Section 6.7 of the Plan.

2.11 "EXCHANGE ACT" means the Securities Exchange Act of 1934, as amended.

2.12 "FAIR MARKET VALUE" means, with respect to the Common Stock, as of any date (or, if no shares were traded or quoted on such date, as of the next preceding date on which there was such a trade or quote): (a) the mean between the reported high and low sale prices of the Common Stock if the Common Stock is listed, admitted to unlisted trading privileges or reported on any foreign or national securities exchange or on the Nasdaq National Market or an equivalent foreign market on which sale prices are reported; (b) if the Common Stock is not so listed, admitted to unlisted trading privileges or reported, the closing bid price as reported by the Nasdaq SmallCap Market, OTC Bulletin Board or the National Quotation Bureau, Inc. or other comparable service; or (c) if the Common Stock is not so listed or reported, such price as the Committee determines in good faith in the exercise of its reasonable discretion. If determined by the Committee, such determination will be final, conclusive and binding for all purposes and on all persons, including, without limitation, the Company, the shareholders of the Company, the Participants and their respective successors-in-interest. No member of the Committee will be liable for any determination regarding the fair market value of the Common Stock that is made in good faith.

2.13 "INCENTIVE AWARD" means an Option, Stock Appreciation Right, Restricted Stock Award or Performance Stock Award granted to an Eligible Recipient pursuant to the Plan.

2.14 "INCENTIVE STOCK OPTION" means a right to purchase Common Stock granted to an Eligible Recipient pursuant to Section 6 of the Plan that qualifies as an "incentive stock option" within the meaning of Section 422 of the Code.

2.15 "NON-STATUTORY STOCK OPTION" means a right to purchase Common Stock granted to an Eligible Recipient pursuant to Section 6 of the Plan that does not

qualify as an Incentive Stock Option.

2.16 "OPTION" means an Incentive Stock Option or a Non-Statutory Stock Option.

2.17 "PARTICIPANT" means an Eligible Recipient who receives one or more Incentive Awards under the Plan.

2.18 "PERFORMANCE CRITERIA" means the performance criteria that may be used by the Committee in granting Performance Stock Awards contingent upon achievement of performance goals, consisting of net sales, operating income, income before income taxes, net income, net income per share (basic or diluted), profitability as measured by return ratios (including return on assets, return on equity, return on investment and return on sales), cash flows, market share,

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cost reduction goals, margins (including one or more of gross, operating and net income margins), stock price, total return to shareholders, economic value added, working capital and strategic plan development and implementation. The Committee may select one criterion or multiple criteria for measuring performance and the measurement may be based upon Company, Subsidiary or business unit performance, either absolute or by relative comparison to other companies or any other external measure of the selected criteria.

2.19 "PERFORMANCE STOCK AWARD" means an award of a right to receive shares of Common Stock granted to an Eligible Recipient pursuant to Section 9 of the Plan contingent upon achievement of Performance Criteria or other objectives during a specified period as provided in Section 9.

2.20 "PREVIOUSLY ACQUIRED SHARES" means shares of Common Stock that are already owned by the Participant or, with respect to any Incentive Award, that are to be issued upon the grant, exercise or vesting of such Incentive Award.

2.21 "RESTRICTED STOCK AWARD" means an award of Common Stock granted to an Eligible Recipient pursuant to Section 8 of the Plan that is subject to the restrictions on transferability and the risk of forfeiture imposed by the provisions of such Section 8.

2.22 "RETIREMENT," unless otherwise defined in the instrument evidencing an Incentive Award or in a written employment, services or other agreement between the Participant and the Company or a Subsidiary, means "Retirement" as defined from time to time for purposes of the Plan by the Committee or by the Company's chief human resources officer or other person performing that function or, if not so defined, means voluntary termination of employment or service by the Participant on or after the date the Participant reaches age 55 with the present intention to leave the Company's industry and/or to leave the general workforce.

2.23 "SECURITIES ACT" means the Securities Act of 1933, as amended.

2.24 "STOCK APPRECIATION RIGHT" means a right granted to an Eligible Recipient pursuant to Section 7 of the Plan to receive a payment from the Company, in the form of stock, cash or a combination of both, equal to the difference between the Fair Market Value of one or more shares of Common Stock and the exercise price of such shares under the terms of such Stock Appreciation Right.

2.25 "SUBSIDIARY" means any entity that is directly or indirectly controlled by the Company or any entity in which the Company has a significant equity interest, as determined by the Committee.

2.26 "TAX DATE" means the date any withholding tax obligation arises under the Code for a Participant with respect to an Incentive Award.

### 3. PLAN ADMINISTRATION.

3.1 THE COMMITTEE. The Plan will be administered by the Board or by a committee of the Board. So long as the Company has a class of its equity securities registered under Section 12 of the Exchange Act, any committee administering the Plan will consist solely of two or more members of the Board

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who are "non-employee directors" within the meaning of Rule 16b-3 under the Exchange Act and, if the Board so determines in its sole discretion, who are "outside directors" within the meaning of Section 162(m) of the Code. Such a committee, if established, will act by majority approval of the members (provided, however, that unanimous approval shall be required with respect to any action taken by written consent), and a majority of the members of such a committee will constitute a quorum. As used in the Plan, "Committee" will refer to the Board or to such a committee, if established. To the extent consistent with applicable corporate law of the Company's jurisdiction of incorporation, the Committee may delegate to any officers of the Company the duties, power and authority of the Committee under the Plan pursuant to such conditions or limitations as the Committee may establish; provided, however, that only the Committee may exercise such duties, power and authority with respect to Eligible Recipients who are subject to Section 16 of the Exchange Act. The Committee may exercise its duties, power and authority under the Plan in its sole discretion without the consent of any Participant or other party, unless the Plan specifically provides otherwise. Each determination, interpretation or other action made or taken by the Committee pursuant to the provisions of the Plan will be conclusive and binding for all purposes and on all persons, and no member of the Committee will be liable for any action or determination made in good faith with respect to the Plan or any Incentive Award granted under the Plan.

### 3.2 AUTHORITY OF THE COMMITTEE.

(a) In accordance with and subject to the provisions of the Plan,

the Committee will have the authority to determine all provisions of Incentive Awards as the Committee may deem necessary or desirable and as consistent with the terms of the Plan, including, without limitation, the following: (i) the Eligible Recipients to be selected as Participants; (ii) the nature and extent of the Incentive Awards to be made to each Participant (including the number of shares of Common Stock to be subject to each Incentive Award, any exercise price, the manner in which Incentive Awards will vest or become exercisable and whether Incentive Awards will be granted in tandem with other Incentive Awards) and the form of written agreement, if any, evidencing such Incentive Award; (iii) the time or times when Incentive Awards will be granted; (iv) the duration of each Incentive Award; and (v) the restrictions and other conditions to which the payment or vesting of Incentive Awards may be subject. In addition, the Committee will have the authority under the Plan in its sole discretion to pay the economic value of any Incentive Award in the form of cash, Common Stock or any combination of both.

(b) Subject to Section 3.2(d), below, the Committee will have the authority under the Plan to amend or modify the terms of any outstanding Incentive Award in any manner, including, without limitation, the authority to modify the number of shares or other terms and conditions of an Incentive Award, extend the term of an Incentive Award, accelerate the exercisability or vesting or otherwise terminate any restrictions relating to an Incentive Award, accept the surrender of any outstanding Incentive Award or, to the extent not previously exercised or vested, authorize the grant of new Incentive Awards in substitution for surrendered Incentive Awards; provided, however that the amended or modified terms are permitted by the Plan as then in effect and that any Participant adversely affected by such amended or modified terms has consented to such amendment or modification.

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(c) In the event of: (i) any reorganization, merger, consolidation, recapitalization, liquidation, reclassification, stock dividend, stock split, combination of shares, rights offering, extraordinary dividend or divestiture (including a spin off) or any other change in corporate structure or shares; (ii) any purchase, acquisition, sale, disposition or write-down of a significant amount of assets or a significant business; (iii) any change in accounting principles or practices, tax laws or other such laws or provisions affecting reported results; (iv) any uninsured catastrophic losses or extraordinary non-recurring items as described in Accounting Principles Board Opinion No. 30 or in management's discussion and analysis of financial performance appearing in the Company's annual report to shareholders for the applicable year; or (v) any other similar change, in each case with respect to the Company or any other entity whose performance is relevant to the grant or vesting of an Incentive Award, the Committee (or, if the Company is not the surviving corporation in

any such transaction, the board of directors of the surviving corporation) may, without the consent of any affected Participant, amend or modify the vesting criteria (including Performance Criteria) of any outstanding Incentive Award that is based in whole or in part on the financial performance of the Company (or any Subsidiary or division or other subunit thereof) or such other entity so as equitably to reflect such event, with the desired result that the criteria for evaluating such financial performance of the Company or such other entity will be substantially the same (in the sole discretion of the Committee or the board of directors of the surviving corporation) following such event as prior to such event; provided, however, that the amended or modified terms are permitted by the Plan as then in effect.

(d) Notwithstanding any other provision of this Plan other than Section 4.3, the Committee may not, without prior approval of the Company's shareholders, seek to effect any re-pricing of any previously granted, "underwater" Option or Stock Appreciation Right by: (i) amending or modifying the terms of the Option or Stock Appreciation Right to lower the exercise price; (ii) canceling the underwater Option or Stock Appreciation Right and granting either (A) replacement Options or Stock Appreciation Rights having a lower exercise price; (B) Restricted Stock Awards; or (C) Performance Stock Awards in exchange; or (iii) repurchasing the underwater Options or Stock Appreciation Rights and granting new Incentive Awards under this Plan. For purposes of this Section 3.2(d), an Option or Stock Appreciation Right will be deemed to be "underwater" at any time when the Fair Market Value of the Common Stock is less than the exercise price of the Option or Stock Appreciation Right.

(e) In addition to the authority of the Committee under Section 3.2(b) and notwithstanding any other provision of the Plan, the Committee may, in its sole discretion, amend the terms of the Plan or Incentive Awards with respect to Participants resident outside of the United States or employed by a non-U.S. Subsidiary in order to comply with local legal requirements, to otherwise protect the Company's or Subsidiary's interests, or to meet objectives of the Plan, and may, where appropriate, establish one or more sub-plans (including the adoption of any required rules and regulations) for the purposes of qualifying for preferred tax treatment under foreign tax laws. The Committee shall have no authority, however, to take action pursuant to this Section 3.2(e): (i) to reserve shares or grant Incentive Awards in

excess of the limitations provided in Section 4.1; (ii) to effect any re-pricing in violation of Section 3.2(d); (iii) to grant Options or Stock Appreciation Rights having an exercise price less than 100% of the Fair Market Value of one share of Common Stock on the date of grant in violation of Section 6.2 or Section 7.2; or (iv) for which shareholder approval would then be required pursuant to Section 422 of the Code or

the rules of any stock exchange on which shares of Common Stock may be listed for trading.

#### 4. SHARES AVAILABLE FOR ISSUANCE.

4.1 MAXIMUM NUMBER OF SHARES AVAILABLE; CERTAIN RESTRICTIONS ON AWARDS. Subject to adjustment as provided in Section 4.3 of the Plan, the maximum number of shares of Common Stock that will be available for issuance under the Plan will be 3,000,000 Notwithstanding any other provisions of the Plan to the contrary, (i) no Participant in the Plan may be granted any Incentive Awards relating to more than 500,000 shares of Common Stock in the aggregate during any 12-month period; and (ii) no more than 1,000,000 shares of Common Stock may be granted as Restricted Stock Awards or Performance Stock Awards under the Plan, with the foregoing limits subject, in each case, to adjustment as provided in Section 4.3 of the Plan.

4.2 ACCOUNTING FOR INCENTIVE AWARDS. Shares of Common Stock that are issued under the Plan or that are subject to outstanding Incentive Awards will be applied to reduce the maximum number of shares of Common Stock remaining available for issuance under the Plan; provided, however, that shares subject to an Incentive Award that lapses, expires, is forfeited (including issued shares forfeited under a Restricted Stock Award) or for any reason is terminated unexercised or unvested or is settled or paid in cash or any form other than shares of Common Stock will automatically again become available for issuance under the Plan. To the extent that the exercise price of any Incentive Award and/or associated tax withholding obligations are paid by tender or attestation as to ownership of Previously Acquired Shares, or to the extent that such tax withholding obligations are satisfied by withholding of shares otherwise issuable upon exercise of the Incentive Award, only the number of shares of Common Stock issued net of the number of shares tendered, attested to or withheld will be applied to reduce the maximum number of shares of Common Stock remaining available for issuance under the Plan. Similarly, any shares of Common Stock that are repurchased by the Company on the open market or in private transactions may be added to the aggregate number of shares available for issuance under the Plan, so long as the aggregate price paid for such repurchased shares does not exceed the cumulative amount received in cash by the Company upon the exercise of Options or issuance of Incentive Awards granted under the Plan.

4.3 ADJUSTMENTS TO SHARES AND INCENTIVE AWARDS. In the event of any reorganization, merger, consolidation, recapitalization, liquidation, reclassification, stock dividend, stock split, combination of shares, rights offering, divestiture or extraordinary dividend (including a spin off) or any other change in the corporate structure or shares of the Company, the Committee (or, if the Company is not the surviving corporation in any such transaction, the board of directors of the surviving corporation) will make appropriate adjustment (which determination will be conclusive) as to the number and kind of securities or other property (including cash) available for issuance or payment



under the Plan and, in order to prevent dilution or enlargement of the rights of Participants, (a) the number and kind of securities or other property (including cash) subject to outstanding Incentive Awards, and (b) the exercise price of outstanding Incentive Awards.

## 5. PARTICIPATION.

Participants in the Plan will be those Eligible Recipients who, in the judgment of the Committee, have contributed, are contributing or are expected to contribute to the achievement of the objectives of the Company or its Subsidiaries. Eligible Recipients may be granted from time to time one or more Incentive Awards, singly or in combination or in tandem with other Incentive Awards, as may be determined by the Committee in its sole discretion. Incentive Awards will be deemed to be granted as of the date specified in the grant resolution of the Committee, which date will be the date of any related agreement with the Participant.

## 6. OPTIONS.

6.1 GRANT. An Eligible Recipient may be granted one or more Options under the Plan, and such Options will be subject to such terms and conditions, consistent with the other provisions of the Plan, as may be determined by the Committee in its sole discretion. The Committee may designate whether an Option is to be considered an Incentive Stock Option or a Non-Statutory Stock Option. To the extent that any Incentive Stock Option granted under the Plan ceases for any reason to qualify as an "incentive stock option" for purposes of Section 422 of the Code, such Incentive Stock Option will continue to be outstanding for purposes of the Plan but will thereafter be deemed to be a Non-Statutory Stock Option.

6.2 EXERCISE PRICE. The per share price to be paid by a Participant upon exercise of an Option will be determined by the Committee in its sole discretion at the time of the Option grant, provided that such price will not be less than 100% of the Fair Market Value of one share of Common Stock on the date of grant (110% of the Fair Market Value if, at the time the Incentive Stock Option is granted, the Participant owns, directly or indirectly, more than 10% of the total combined voting power of all classes of stock of the Company or any parent or subsidiary corporation of the Company).

6.3 EXERCISABILITY AND DURATION. An Option will become exercisable at such times and in such installments and upon such terms and conditions as may be determined by the Committee in its sole discretion at the time of grant, including without limitation (i) the achievement of one or more of the Performance Criteria; and/or that (ii) the Participant remain in the continuous employment or service with the Company or a Subsidiary for a certain period; provided, however, that no Option may be exercisable after 10 years from its date of grant.

6.4 PAYMENT OF EXERCISE PRICE. The total purchase price of the shares to be purchased upon exercise of an Option will be paid entirely in cash (including

check, bank draft or money order); provided, however, that the Committee, in its sole discretion and upon terms and conditions established by the Committee, may allow such payments to be made, in whole or in part, by tender of a Broker Exercise Notice, by tender, or attestation as to ownership, of Previously Acquired Shares that have been held for the period of time necessary to avoid a charge to the Company's earnings for financial reporting purposes and that are otherwise acceptable to the Committee, or by a combination of such methods. For

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purposes of such payment, Previously Acquired Shares tendered or covered by an attestation will be valued at their Fair Market Value on the exercise date.

6.5 MANNER OF EXERCISE. An Option may be exercised by a Participant in whole or in part from time to time, subject to the conditions contained in the Plan and in the agreement evidencing such Option, by delivery in person, by facsimile or electronic transmission or through the mail of written notice of exercise to the Company at its principal executive office in Minneapolis, Minnesota (or to the Company's designee as may be established from time to time by the Company and communicated to Participants) and by paying in full the total exercise price for the shares of Common Stock to be purchased in accordance with Section 6.4 of the Plan.

6.6 AGGREGATE LIMITATION OF STOCK SUBJECT TO INCENTIVE STOCK OPTIONS. To the extent that the aggregate Fair Market Value (determined as of the date an Incentive Stock Option is granted) of the shares of Common Stock with respect to which incentive stock options (within the meaning of Section 422 of the Code) are exercisable for the first time by a Participant during any calendar year (under the Plan and any other incentive stock option plans of the Company or any subsidiary or parent corporation of the Company (within the meaning of the Code)) exceeds \$100,000 (or such other amount as may be prescribed by the Code from time to time), such excess Options will be treated as Non-Statutory Stock Options. The determination will be made by taking incentive stock options into account in the order in which they were granted. If such excess only applies to a portion of an Incentive Stock Option, the Committee, in its discretion, will designate which shares will be treated as shares to be acquired upon exercise of an Incentive Stock Option.

#### 6.7 NON-DISCRETIONARY GRANT OF OPTIONS TO NON-EMPLOYEE DIRECTORS.

(a) Each non-employee director on the effective date of the Plan (or, if first elected after the effective date of the Plan, on the date the non-employee director is first elected) shall be awarded an Option to purchase up to 10,000 shares of Common Stock (or such lesser number of shares as may be determined by the Committee from time to time and subject to adjustment upon changes in capitalization of the Company as provided in Section 4.3 above). As of the close of business on each successive annual shareholders' meeting date after the date of the original award, each non-employee director continuing in service on the Board of Directors of the Company shall be granted an additional Option



to purchase up to 10,000 shares of Common Stock (or such lesser number of shares as may be determined by the Committee from time to time and subject to adjustment upon changes in capitalization of the Company as provided in Section 4.3 above). All Options granted under this Section 6.7 of the Plan shall be Non-Statutory Stock Options not entitled to special tax treatment under Section 422 of the Internal Revenue Code of 1986, as amended.

(b) The per share price to be paid by the non-employee director upon exercise of an Option granted under this Section 6.7 will be equal to 100% of the Fair Market Value of the Common Stock on the date of grant.

(c) Subject to continuing service by the non-employee director on the Board of Directors of the Company, each Option granted under this Section 6.7 will vest one year after the date the Option is granted. If,

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for any reason, a non-employee director ceases to serve on the Board prior to the date an Option vests, such Option shall be forfeited and all further rights of the non-employee director to or with respect to such Option shall terminate. Each Option granted under this Section 6.7 shall expire ten (10) years from the date of grant, subject to earlier termination of the Option pursuant to the provisions of Section 10 of this Plan.

## 7. STOCK APPRECIATION RIGHTS.

7.1 GRANT. An Eligible Recipient may be granted one or more Stock Appreciation Rights under the Plan, and such Stock Appreciation Rights will be subject to such terms and conditions, consistent with the other provisions of the Plan, as may be determined by the Committee in its sole discretion.

7.2 EXERCISE PRICE. The exercise price of a Stock Appreciation Right will be determined by the Committee, in its discretion, at the date of grant but may not be less than 100% of the Fair Market Value of one share of Common Stock on the date of grant.

7.3 EXERCISABILITY AND DURATION. A Stock Appreciation Right will become exercisable at such time and in such installments as may be determined by the Committee in its sole discretion at the time of grant; provided, however, that no Stock Appreciation Right may be exercisable after 10 years from its date of grant. A Stock Appreciation Right will be exercised by giving notice in the same manner as for Options, as set forth in Section 6.5 of the Plan.

## 8. RESTRICTED STOCK AWARDS.

8.1 GRANT. An Eligible Recipient may be granted one or more Restricted Stock Awards under the Plan, and such Restricted Stock Awards will be subject to

such terms and conditions, consistent with the other provisions of the Plan, as may be determined by the Committee in its sole discretion. The Committee may impose such restrictions or conditions, not inconsistent with the provisions of the Plan, to the vesting of such Restricted Stock Awards as it deems appropriate, including, without limitation, (i) the achievement of one or more of the Performance Criteria; and/or that (ii) the Participant remain in the continuous employment or service with the Company or a Subsidiary for a certain period. Notwithstanding the foregoing, no Restricted Stock Award shall vest within a period of less than three (3) years from the date of grant of the Restricted Stock Award.

8.2 RIGHTS AS A STOCKHOLDER; TRANSFERABILITY. Except as provided in Sections 8.1, 8.3, 8.4 and 13.3 of the Plan, upon a Participant becoming the holder of record of shares of Common Stock issued under a Restricted Stock Award pursuant to this Section 8, the Participant will have all voting, dividend, liquidation and other rights with respect to such shares (other than the right to sell or transfer such shares) as if such Participant were a holder of record of shares of unrestricted Common Stock.

8.3 DIVIDENDS AND DISTRIBUTIONS. Unless the Committee determines otherwise in its sole discretion (either in the agreement evidencing the Restricted Stock Award at the time of grant or at any time after the grant of the Restricted Stock Award), any dividends or distributions (other than regular quarterly cash dividends) paid with respect to shares of Common Stock subject to

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the unvested portion of a Restricted Stock Award will be subject to the same restrictions as the shares to which such dividends or distributions relate. The Committee will determine in its sole discretion whether any interest will be paid on such dividends or distributions.

8.4 ENFORCEMENT OF RESTRICTIONS. To enforce the restrictions referred to in this Section 8, the Committee may place a legend on the stock certificates referring to such restrictions and may require the Participant, until the restrictions have lapsed, to keep the stock certificates, together with duly endorsed stock powers, in the custody of the Company or its transfer agent, or to maintain evidence of stock ownership, together with duly endorsed stock powers, in a certificateless book entry stock account with the Company's transfer agent. Alternatively, Restricted Stock Awards may be held in non-certificated form pursuant to such terms and conditions as the Company may establish with its registrar and transfer agent and/or any third-party administrator designated by the Company to hold Restricted Stock Awards on behalf of Participants.

## 9. PERFORMANCE STOCK AWARDS.

An Eligible Recipient may be granted one or more Performance Stock Awards under the Plan, and the issuance of shares of Common Stock pursuant to such Performance Stock Awards will be subject to such terms and conditions, if

any, consistent with the other provisions of the Plan, as may be determined by the Committee in its sole discretion, including, but not limited to, the achievement of one or more of the Performance Criteria. Notwithstanding the foregoing, no Performance Stock Award shall vest within a period of less than one (1) year from the date of grant of the Performance Stock Award.

10. EFFECT OF TERMINATION OF EMPLOYMENT OR OTHER SERVICE.

10.1 TERMINATION DUE TO DEATH OR DISABILITY. Unless otherwise expressly provided by the Committee in its sole discretion in the agreement evidencing an Incentive Award, and subject to Section 10.5 of the Plan, in the event a Participant's employment or other service with the Company and all Subsidiaries is terminated by reason of death or Disability:

(a) All outstanding Options and Stock Appreciation Rights then held by the Participant will become immediately exercisable in full and will remain exercisable for a period of two years after such termination (but in no event after the expiration date of any such Option or Stock Appreciation Right);

(b) All Restricted Stock Awards then held by the Participant will become fully vested; and

(c) Any conditions with respect to the issuance of shares of Common Stock pursuant to Performance Stock Awards will lapse.

10.2 TERMINATION DUE TO RETIREMENT. Unless otherwise expressly provided by the Committee in its sole discretion in the agreement evidencing an Incentive Award, and subject to Section 10.5 of the Plan, in the event a Participant's employment or other service with the Company and all Subsidiaries is terminated by reason of Retirement, then any Incentive Awards held by the Participant that

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vest over one or more incremental period or periods of more than one year in each incremental period shall be vested on a pro rata basis at the date of Retirement of the Participant, and:

(a) All outstanding Options and Stock Appreciation Rights then held by the Participant will, to the extent exercisable as of the date of Retirement, remain exercisable in full for a period of one year after the date of Retirement (but in no event after the expiration date of any such Option or Stock Appreciation Right). Options and Stock Appreciation Rights not exercisable as of the date of Retirement will be terminated and forfeited.

(b) All Restricted Stock Awards then held by the Participant that have not vested as of the date of Retirement will be terminated and forfeited; and

(c) All outstanding Performance Stock Awards then held by the Participant will be terminated and forfeited.

10.3 TERMINATION FOR REASONS OTHER THAN DEATH, DISABILITY OR RETIREMENT. Unless otherwise expressly provided by the Committee in its sole discretion in the agreement evidencing an Incentive Award, and subject to Section 10.5 of the Plan, in the event a Participant's employment or other service is terminated with the Company and all Subsidiaries for any reason other than death, Disability or Retirement, or a Participant is in the employment of a Subsidiary and the Subsidiary ceases to be a Subsidiary of the Company (unless the Participant continues in the employment of the Company or another Subsidiary):

(a) All outstanding Options and Stock Appreciation Rights then held by the Participant will, to the extent exercisable as of such termination, remain exercisable in full for a period of three months after such termination (but in no event after the expiration date of any such Option or Stock Appreciation Right). Options and Stock Appreciation Rights not exercisable as of such termination will be terminated and forfeited.

(b) All Restricted Stock Awards then held by the Participant that have not vested as of such termination will be terminated and forfeited; and

(c) All outstanding Performance Stock Awards then held by the Participant will be terminated and forfeited.

10.4 MODIFICATION OF RIGHTS UPON TERMINATION. Notwithstanding the other provisions of this Section 10, upon a Participant's termination of employment or other service with the Company and all Subsidiaries, the Committee may, in its sole discretion (which may be exercised at any time on or after the date of grant, including following such termination), cause Options and/or Stock Appreciation Rights (or any part thereof) then held by such Participant to become or continue to become exercisable and/or remain exercisable following such termination of employment, and Restricted Stock Awards and/or Performance Stock Awards then held by such Participant to vest and/or continue to vest or become free of restrictions and conditions to issuance, as the case may be, following such termination of employment, in each case in the manner determined

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by the Committee; provided, however, that no Option or Stock Appreciation Right may remain exercisable beyond its expiration date.

10.5 EFFECTS OF ACTIONS CONSTITUTING CAUSE. Notwithstanding anything in the Plan to the contrary, in the event that a Participant is determined by the Committee, acting in its sole discretion, to have committed any action which would constitute Cause as defined in Section 2.3, irrespective of whether such action or the Committee's determination occurs before or after termination of such Participant's employment or other service with the Company or any

Subsidiary, all rights of the Participant under the Plan and any agreements evidencing an Incentive Award then held by the Participant shall terminate and be forfeited without notice of any kind. The Company may defer the exercise of any Option or Stock Appreciation Right, the vesting of any Restricted Stock Award or the issuance of any shares of Common Stock pursuant to any Performance Stock Award for a period of up to forty-five (45) days in order for the Committee to make any determination as to the existence of Cause.

10.6 DETERMINATION OF DATE OF TERMINATION. Unless the Committee otherwise determines in its sole discretion, a Participant's employment or other service will, for purposes of the Plan, be deemed to have terminated on the date recorded on the personnel or other records of the Company or the Subsidiary for which the Participant provides employment or other services, as determined by the Committee in its sole discretion based upon such records.

11. PAYMENT OF WITHHOLDING TAXES.

11.1 GENERAL RULES. The Company is entitled to (a) withhold and deduct from future wages of the Participant (or from other amounts that may be due and owing to the Participant from the Company or a Subsidiary), or make other arrangements for the collection of, all legally required amounts necessary to satisfy any and all federal, foreign, state and local withholding and employment related tax requirements attributable to an Incentive Award, including, without limitation, the grant, exercise or vesting of, or payment of dividends with respect to, an Incentive Award or a disqualifying disposition of stock received upon exercise of an Incentive Stock Option, or (b) require the Participant promptly to remit the amount of such withholding to the Company before taking any action, including issuing any shares of Common Stock, with respect to an Incentive Award.

11.2 SPECIAL RULES. The Committee may, in its sole discretion and upon terms and conditions established by the Committee, permit or require a Participant to satisfy, in whole or in part, any withholding or employment related tax obligation described in Section 11.1 of the Plan by electing to tender, or by attestation as to ownership of, Previously Acquired Shares that have been held for the period of time necessary to avoid a charge to the Company's earnings for financial reporting purposes and that are otherwise acceptable to the Committee, by delivery of a Broker Exercise Notice or a combination of such methods. For purposes of satisfying a Participant's withholding or employment-related tax obligation, Previously Acquired Shares tendered or covered by an attestation will be valued at their Fair Market Value.

12. CHANGE IN CONTROL.

12.1 CHANGE IN CONTROL. For purposes of this Section 12, a "Change in Control" of the Company shall mean (a) the sale, lease, exchange or other transfer of all or substantially all of the assets of the Company (in one

transaction or in a series of related transactions) to a corporation that is not controlled by the Company, (b) the approval by the shareholders of the Company of any plan or proposal for the liquidation or dissolution of the Company, or (c) a change in control of a nature that would be required to be reported (assuming such event has not been "previously reported") in response to Item 1(a) of the Current Report on Form 8-K, as in effect on the effective date of the Plan, pursuant to Section 13 or 15(d) of the Exchange Act, whether or not the Company is then subject to such reporting requirement; provided that, without limitation, such a Change in Control shall be deemed to have occurred at such time as (x) any Person becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act) directly or indirectly, of 50% or more of the combined voting power of the Company's outstanding securities ordinarily having the right to vote at elections of directors or (y) individuals who constitute the Board of Directors on the effective date of the Plan cease for any reason to constitute at least a majority thereof, provided that any person becoming a director subsequent to the effective date of the Plan whose election, or nomination for election by the Company's shareholders, was approved by a vote of at least a majority of the directors comprising the Board of Directors on the effective date of the Plan (either by a specific vote or by approval of the proxy statement of the Company in which such person is named as a nominee for director, without objection to such nomination) shall be, for purposes of this clause (y), considered as though such person were a member of the Board of Directors on the effective date of the Plan.

12.2 ACCELERATION OF VESTING. Without limiting the authority of the Committee under Sections 3.2 and 4.3 of the Plan, if a Change in Control of the Company occurs, then, unless otherwise provided by the Committee in its sole discretion either in the agreement evidencing an Incentive Award at the time of grant or at any time after the grant of an Incentive Award, (a) all outstanding Options and Stock Appreciation Rights will become immediately exercisable in full and will remain exercisable for the remainder of their terms, regardless of whether the Participant to whom such Options or Stock Appreciation Rights have been granted remains in employment or service with the Company or any Subsidiary; (b) all outstanding Restricted Stock Awards will become immediately fully vested and non-forfeitable; and (c) all outstanding Performance Stock Awards will vest and/or continue to vest in the manner determined by the Committee and set forth in the respective agreements evidencing such Performance Stock Awards.

12.3 CASH PAYMENT FOR OPTIONS. If a Change in Control of the Company occurs, then the Committee, if approved by the Committee in its sole discretion either in an agreement evidencing an Incentive Award at the time of grant or at any time after the grant of an Incentive Award, and without the consent of any Participant effected thereby, may determine that some or all Participants holding outstanding Options will receive, with respect to some or all of the shares of Common Stock subject to such Options, as of the effective date of any such Change in Control of the Company, cash in an amount equal to the excess of the Fair Market Value of such shares immediately prior to the effective date of such Change in Control of the Company over the exercise price per share of such Options.



### 13. RIGHTS OF ELIGIBLE RECIPIENTS AND PARTICIPANTS; TRANSFERABILITY.

13.1 EMPLOYMENT. Nothing in the Plan will interfere with or limit in any way the right of the Company or any Subsidiary to terminate the employment of any Eligible Recipient or Participant at any time, nor confer upon any Eligible Recipient or Participant any right to continue in employment with the Company or any Subsidiary.

13.2 RIGHTS AS A STOCKHOLDER. As a holder of Incentive Awards (other than Restricted Stock Awards), a Participant will have no rights as a shareholder unless and until such Incentive Awards are exercised for, or paid in the form of, shares of Common Stock and the Participant becomes the holder of record of such shares. Except as otherwise expressly provided in the Plan and except as the Committee may determine in its sole discretion, no adjustment will be made for dividends or distributions with respect to such Incentive Awards as to which there is a record date preceding the date the Participant becomes the holder of record of such shares.

### 13.3 RESTRICTIONS ON TRANSFER.

(a) Except pursuant to testamentary will or the laws of descent and distribution or as otherwise expressly permitted by subsections (b) and (c) below, no right or interest of any Participant in an Incentive Award prior to the exercise (in the case of Options or Stock Appreciation Rights) or vesting or issuance (in the case of Restricted Stock Awards and Performance Stock Awards) of such Incentive Award will be assignable or transferable, or subjected to any lien, during the lifetime of the Participant, either voluntarily or involuntarily, directly or indirectly, by operation of law or otherwise.

(b) A Participant will be entitled to designate a beneficiary to receive an Incentive Award upon such Participant's death, and in the event of such Participant's death, payment of any amounts due under the Plan will be made to, and exercise of any Options or Stock Appreciation Rights (to the extent permitted pursuant to Section 10 of the Plan) may be made by, such beneficiary. If a deceased Participant has failed to designate a beneficiary, or if a beneficiary designated by the Participant fails to survive the Participant, payment of any amounts due under the Plan will be made to, and exercise of any Options or Stock Appreciation Rights (to the extent permitted pursuant to Section 10 of the Plan) may be made by, the Participant's legal representatives, heirs and legatees. If a deceased Participant has designated a beneficiary and such beneficiary survives the Participant but dies before complete payment of all amounts due under the Plan or exercise of all exercisable Options or Stock Appreciation Rights, then such payments will be made to, and the exercise of such Options or Stock Appreciation Rights may be

made by, the legal representatives, heirs and legatees of the beneficiary.

(c) Upon a Participant's request, the Committee may, in its sole discretion, permit a transfer of all or a portion of a Non-Statutory Stock Option or Stock Appreciation Right, other than for value, to such Participant's child, stepchild, grandchild, parent, stepparent, grandparent, spouse, former spouse, sibling, niece, nephew, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, any person sharing such Participant's household (other than a tenant or employee), a trust in which any of the foregoing have more than fifty percent (50%) of the beneficial

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interests, a foundation in which any of the foregoing (or the Participant) control the management of assets, and any other entity in which these persons (or the Participant) own more than fifty percent (50%) of the voting interests. Any permitted transferee will remain subject to all the terms and conditions applicable to the Participant prior to the transfer. A permitted transfer may be conditioned upon such requirements as the Committee may, in its sole discretion, determine, including, but not limited to execution and/or delivery of appropriate acknowledgements, opinion of counsel, or other documents by the transferee.

13.4 NON-EXCLUSIVITY OF THE PLAN. Nothing contained in the Plan is intended to modify or rescind any previously approved compensation plans or programs of the Company or create any limitations on the power or authority of the Board to adopt such additional or other compensation arrangements as the Board may deem necessary or desirable.

#### 14. SECURITIES LAW AND OTHER RESTRICTIONS.

Notwithstanding any other provision of the Plan or any agreements entered into pursuant to the Plan, the Company will not be required to issue any shares of Common Stock under this Plan, and a Participant may not sell, assign, transfer or otherwise dispose of shares of Common Stock issued pursuant to Incentive Awards granted under the Plan, unless (a) there is in effect with respect to such shares a registration statement under the Securities Act and any applicable securities laws of a state or foreign jurisdiction or an exemption from such registration under the Securities Act and applicable state or foreign securities laws, and (b) there has been obtained any other consent, approval or permit from any other U.S. or foreign regulatory body which the Committee, in its sole discretion, deems necessary or advisable. The Company may condition such issuance, sale or transfer upon the receipt of any representations or agreements from the parties involved, and the placement of any legends on certificates representing shares of Common Stock, as may be deemed necessary or advisable by the Company in order to comply with such securities law or other restrictions.



15. PERFORMANCE-BASED COMPENSATION PROVISIONS.

The Committee, when it is comprised solely of two or more outside directors meeting the requirements of Section 162(m) of the Code ("Section 162(m)"), in its sole discretion, may designate whether any Incentive Awards are intended to be "performance-based compensation" within the meaning of Section 162(m). Any Incentive Awards so designated will, to the extent required by Section 162(m), be conditioned upon the achievement of one or more Performance Criteria, and such Performance Criteria will be established by the Committee within the time period prescribed by, and will otherwise comply with the requirements of, Section 162(m) giving due regard to the disparate treatment under Section 162(m) of Options and Stock Appreciation Rights (where compensation is determined based solely on an increase in the value of the underlying stock after the date of grant or award), as compared to other forms of compensation, including Restricted Stock Awards and Performance Stock Awards. The Committee shall also certify in writing that such Performance Criteria have been met prior to payment of compensation to the extent required by Section 162(m).

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16. PLAN AMENDMENT, MODIFICATION AND TERMINATION.

The Board may suspend or terminate the Plan or any portion thereof at any time. In addition to the authority of the Committee to amend the Plan under Section 3.2(e), the Board may amend the Plan from time to time in such respects as the Board may deem advisable in order that Incentive Awards under the Plan will conform to any change in applicable laws or regulations or in any other respect the Board may deem to be in the best interests of the Company; provided, however, that no such amendments to the Plan will be effective without approval of the Company's shareholders if: (i) shareholder approval of the amendment is then required pursuant to Section 422 of the Code or the rules of the primary stock exchange or stock market on which the Common Stock is then traded; or (ii) such amendment would: (A) modify Section 3.2(d) hereof; (B) materially increase benefits accruing to Participants; (C) increase the aggregate number of shares issued or issuable under the Plan; or (D) modify the eligibility requirements for Participants in the Plan. No termination, suspension or amendment of the Plan may adversely affect any outstanding Incentive Award without the consent of the affected Participant; provided, however, that this sentence will not impair the right of the Committee to take whatever action it deems appropriate under Sections 3.2(c), 4.3 and 12 of the Plan.

17. EFFECTIVE DATE AND DURATION OF THE PLAN.

The Plan is effective as of the Effective Date. The Plan will terminate at midnight on May 20, 2014, and may be terminated prior to such time by Board action. No Incentive Award will be granted after termination of the Plan. Incentive Awards outstanding upon termination of the Plan may continue to be

exercised, or become free of restrictions, according to their terms.

18. MISCELLANEOUS.

18.1 GOVERNING LAW. Except to the extent expressly provided herein or in connection with other matters of corporate governance and authority (all of which shall be governed by the laws of the Company's jurisdiction of incorporation), the validity, construction, interpretation, administration and effect of the Plan and any rules, regulations and actions relating to the Plan will be governed by and construed exclusively in accordance with the laws of the State of Minnesota, notwithstanding the conflicts of laws principles of any jurisdictions.

18.2 SUCCESSORS AND ASSIGNS. The Plan will be binding upon and inure to the benefit of the successors and permitted assigns of the Company and the Participants.