UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark one)

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

For the Fiscal Year Ended January 3, 2009

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

For the transition period from _________ to _________.

Commission File No. 0-25121

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.)
9800 59th Avenue North **Minneapolis, Minnesota** (Address of principal executive offices)	**55442** (Zip code)

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

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

Title of each class	Name of each exchange on which registered
Common Stock, par value $.01 per share	The NASDAQ Stock Market LLC (NASDAQ Global Select Market)

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined by Rule 405 of the Securities Act.
YES o NO x

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
YES o NO x

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 o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	o	Accelerated filer	x
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller reporting company	o

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). YES o NO x

The aggregate market value of the common equity held by non-affiliates of the Registrant as of June 28, 2008, was $68,500,000 (based on the last reported sale price of the Registrant's common stock on that date as reported by NASDAQ).

As of January 31, 2009, there were 45,300,669 shares of the Registrant's common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's proxy statement to be furnished to shareholders in connection with its 2009 Annual Meeting of Shareholders are incorporated by reference in Part III, Items 10-14 of this Annual Report on Form 10-K.

As used in this Form 10-K, the terms "we," "us," "our," the "company" and "Select Comfort" mean Select Comfort Corporation and its subsidiaries and the term "common stock" means our common stock, par value $0.01 per share.

As used in this Form 10-K, the term "bedding" includes mattresses, box springs and foundations and does not include bedding accessories, such as sheets, pillows, headboards, frames, mattress pads and related products.

Select Comfort®, Sleep Number®, Comfort Club®, Sleep Better on Air®, The Sleep Number Bed by Select Comfort (logo)®, Select Comfort (logo with double arrow design)®, Firmness Control System™, Precision Comfort®, Corner Lock™, Intralux®, The Sleep Number Store by Select Comfort (logo)®, You can only find your Sleep Number® setting on a Sleep Number Bed by Select Comfort™, Select Comfort Creator of the Sleep Number Bed®, What's Your Sleep Number® setting?, Grand King®, Sleep Number SofaBed™, Personalized Warmth Collection®, GridZone®, and our stylized logos are trademarks and/or service marks of Select Comfort. This Form 10-K may also contain trademarks, trade names and service marks that are owned by other persons or entities.

Our fiscal year ends on the Saturday closest to December 31, and, unless the context otherwise requires, all references to years in this Form 10-K refer to our fiscal years. Our fiscal year is based on a 52- or 53-week year. All years presented in this Form 10-K are 52 weeks, except for the 2008 fiscal year ended January 3, 2009 and the 2003 fiscal year ended January 3, 2004, which are 53-week years.

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PART I

This Annual Report on Form 10-K contains or incorporates by reference certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. For this purpose, any statements contained in or incorporated by reference into this Annual Report on Form 10-K that are not statements of historical fact may be deemed to be forward-looking statements, including but not limited to projections of revenues, results of operations, financial condition or other financial items; any statements of plans, strategies and objectives of management for future operations; any statements regarding proposed new products, services or developments; any statements regarding future economic conditions, prospects or performance; statements of belief and any statement or assumptions underlying any of the foregoing. In addition, we or others on our behalf may make forward-looking statements from time to time in oral presentations, including telephone conferences and/or Web casts open to the public, in press releases or reports, on our Internet Web site or otherwise. We try to identify forward-looking statements in this report and elsewhere by using words such as "may," "will," "should," "could," "expect," "anticipate," "believe," "estimate," "plan," "project," "predict," "intend," "potential," "continue" or the negative of these or similar terms.

Our forward-looking statements speak only as of the date made and by their nature involve substantial risks and uncertainties. Our actual results may differ materially depending on a variety of factors, including the items discussed in greater detail below under the caption "Risk Factors." These risks and uncertainties are not exclusive and further information concerning the company and our business, including factors that potentially could materially affect our financial results or condition, may emerge from time to time, including factors that we may consider immaterial or do not anticipate at this time.

We wish to caution readers not to place undue reliance on any forward-looking statement and to recognize that forward-looking statements are predictions of future results, which may not occur as anticipated. We assume no obligation to update forward-looking statements to reflect actual results or changes in factors or assumptions affecting such forward-looking statements. We advise you, however, to consult any further disclosures we make on related subjects in our quarterly reports on Form 10-Q and current reports on Form 8-K that we file with or furnish to the Securities and Exchange Commission.

ITEM 1. BUSINESS

Our Business

Overview

Select Comfort Corporation was founded as a Minnesota-based corporation in 1987 by an entrepreneur who developed and manufactured adjustable firmness mattresses after considering other alternatives such as innerspring and water mattresses. Select Comfort has evolved from a specialty, niche direct marketer, to a nationwide multi-channel business with fiscal 2008 net sales of $609 million.

Our principal business is to develop, manufacture, market and distribute premium quality, adjustable-firmness beds and other sleep-related accessory products. 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 have a mission-driven culture focused on serving the needs of our customers. Our mission is to improve people's lives through better sleep. Our goal is to educate our consumers on the importance of a better night's sleep and the unique benefits of our products.

In 1998, Select Comfort became a publicly-traded company and is listed on The NASDAQ Stock Market LLC (NASDAQ Global Select Market) under the symbol "SCSS." When used herein, the terms "Select Comfort," "Company," "we," "us" and "our" refer to Select Comfort Corporation, including consolidated subsidiaries.

Competitive Strengths

Differentiated, Superior Product

The unique benefits of our proprietary Sleep Number bed have been validated through clinical sleep research. Clinical sleep research has shown that people who sleep on a Sleep Number bed generally fall asleep faster, experience deeper sleep with fewer disturbances and experience greater relief from back pain than those sleeping on a traditional innerspring mattress. The

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proprietary air-chamber technology of our Sleep Number bed allows adjustable firmness of the mattress at the touch of a button. Our dual chamber technology (two independent air chambers) allows consumers to adjust the firmness on either side of the bed to meet each person's individual preference.

Distinctive Brand

In 2001, we created the Sleep Number brand. This branding strategy allows our marketing communications to focus on our bed's distinguishing and proprietary features – adjustable firmness and support for personalized comfort. This is represented by the digital Sleep Number display on the bed's hand-held remote control, with a brand message hierarchy as follows:

- A Sleep Number® setting represents an ideal level of mattress comfort, firmness and support; and
- You can only find your Sleep Number® setting on a Sleep Number Bed by Select Comfort™.

Controlled Selling Environment

Over 90% of our sales are generated through our company-controlled distribution channels – Retail, Direct Marketing and E-Commerce. Our nationwide chain of retail stores provides a unique mattress shopping experience and offers a relaxed environment designed to provide education on the importance of sleep and the products that best fit consumers' needs. Controlling the selling process enables us to ensure that the unique benefits of our products are effectively communicated to consumers. Our multiple touch-points of service, including sales, delivery and post-sale service, provide several opportunities to communicate with our customers, reinforcing the sale and enabling us to understand and respond quickly to consumer trends and preferences.

Integrated Business Process

We are a vertically-integrated business from production through sales and delivery of our products, which allows us to control quality, cost, price and presentation. The modular design of our Sleep Number bed allows a just-in-time, build-to-order production process which requires minimal inventory in our stores and manufacturing plants, resulting in reduced working capital levels. This just-in-time production process also allows our stores to serve primarily as showrooms, without requiring significant product storage capacity.

Vision and Strategy

For 2007, we ranked as the 5th largest mattress manufacturer according to the June 16, 2008 edition of *Furniture/Today*, with a 6% market share of industry revenue and 2% market share of industry units. We ranked as the leading U.S. bedding retailer, according to the *Top-25 Bedding Retailers* report in the August 11, 2008 edition of *Furniture/Today*. Our vision is to be a leading brand in the bedding industry.

We are executing against a defined strategy which focuses on the following key components:

- Building brand awareness and increasing store traffic through effective marketing programs;
- Prudently managing our business in the current economic environment through disciplined controls over costs and cash;
- Accelerating product innovation to lead the industry in innovative sleep products; and
- Leveraging our infrastructure in order to facilitate long-term profitability.

Building Brand Awareness

Our most significant growth driver has been building brand awareness. The Sleep Number brand has been integrated into all of our sales channels and throughout our internal and external communication programs. We utilize a media mix that includes television, radio and print advertising in support of our Sleep Number marketing campaign with increasing use of Internet advertising and paid search in our media mix.

We also sell to commercial partners which increases awareness of our brand through media exposure, product sales and word-of-mouth. These commercial partners include the QVC television shopping channel, the luxury motor home market, selected mattress retailers and Radisson Hotels and Resorts® in the U.S., Canada and the Caribbean.

As of January 3, 2009 we operated 471 company-owned stores in the U.S. In the current economic environment, we are evaluating and reducing our store base, and expect to end 2009 with no more than 420 stores. We may further reduce our store base in 2009 and 2010. We do not expect to expand our store base until we begin generating comparable-store sales growth on a consistent basis. We supplement our company-controlled distribution channels with sales through a limited number of leading home furnishings and specialty bedding retailers.

In 2005, we expanded our distribution network outside the U.S. with a retail partner relationship in Canada. In 2008, the Canadian retail partner relationship grew to 134 doors. During 2007, we formed a strategic alliance with two Australian-based companies to manufacture and distribute Sleep Number beds and accessories in Australia and New Zealand. Our international distribution network was not a significant part of our total distribution network and we do not plan to expand our international distribution during 2009.

Prudently Managing Our Business

We generated positive net income for six consecutive years from 2002 through 2007. Our 2008 operating results were significantly affected by the industry-wide decrease in consumer spending and we realized a net loss of $70.2 million, including $34.6 million of pre-tax asset impairment charges and a $26.8 million pre-tax charge for a deferred tax valuation allowance.

We have taken significant actions to improve our operating results and maintain our liquidity in the current challenging macro-economic environment, including: corporate workforce reductions, reduced capital spending, executing plans to close stores, supply chain cost reduction initiatives, reduced media spending, reductions in fixed and discretionary marketing and selling expenses, and ceasing all activities associated with the implementation of SAP®-based information technology applications. We are also introducing lower product price points and initiating an enhanced promotional strategy designed to stabilize sales. Additionally, we are exploring a range of strategic and financing alternatives to enhance our financial flexibility and improve our liquidity.

Accelerating Innovation

Our goal is to lead the industry in innovative sleep products. We have historically introduced new features and benefits to our Sleep Number beds every two to three years, through a pipeline of research and development (“R&D”) activities. During 2007, we refreshed our entire line of bed models and will do so again in 2009. Our new models emphasize enhanced comfort-layer materials, and several feature advancements in temperature balancing technology. We believe the new line represents the highest-quality, most technologically advanced beds we have ever produced.

Our 2008 innovations included: (i) the launch of the Sleep Number memory foam bed which combines memory foam conforming comfort with the ability to adjust firmness and provide personalized comfort, and (ii) the Sleep Number p6 bed that has enhanced layers of softness and breathable fabrics. The two new mattress models fill-in key price points in our product line-up.

Leveraging our Infrastructure

Our vertically-integrated business model provides multiple sources for efficiency and leverage. Our goal of sustaining improved performance over a multi-year period is based on achieving scale efficiencies (fixed cost utilization) and cost containment initiatives. We also have an ongoing focus on productivity gains through a variety of programs, including the optimization of our hub and spoke network, value engineering, marketing and sales initiatives, and a Six Sigma initiative to improve product and service quality.

Our Products

Mattresses

We offer Sleep Number beds in three series to help consumers choose the bed that is best for them.

- The Sleep Number bed Classic Series is the classic design with personal adjustability at an affordable price. The series includes the Sleep Number c2, c3 and c4 beds.
- The Sleep Number bed Performance Series includes our most popular beds, featuring enhanced performance, comfort and a great value. The series includes the Sleep Number p5, p6 and p7 beds.

- The Sleep Number bed Innovation Series is the premier experience in personalized comfort combined with leading-edge innovations in sleep technology. The series includes the Sleep Number i8, i9 and i10 beds.

The Sleep Number bed series are available through our U.S. company-owned distribution channels. Each bed series comes in standard mattress sizes, ranging from twin to king, as well as some specialty mattress sizes. Our bed series vary in features, functionality and price. As you move up the line, the Sleep Number bed series offer enhanced features and benefits, including higher-quality fabrics, additional cushion and padding, higher overall mattress profiles, quieter Firmness Control Systems with additional functions, temperature balancing fabrics, and wireless remote controls as a standard feature.

The contouring support of our Sleep Number beds is optimized when used with our specially designed, proprietary foundation. This durable foundation, used in place of a box spring, is a modular design that can be disassembled and easily moved through staircases, hallways and other tight spaces.

Our U.S. mattress price points range from approximately $699 for the entry-level c2 queen-size mattress to $3,999 for the luxurious Sleep Number i10 queen-size mattress. Our most popular model is the p5 queen-size mattress which sells for approximately $1,699. Actual prices are frequently lower than those quoted due to promotional offerings.

Our unique product design allows us to ship our beds in a modular format to customers throughout the U.S. by United Parcel Service (“UPS”). For an additional fee, customers can take advantage of our home delivery service, which includes bed assembly and optional mattress removal services.

We also manufacture our Sleep Number beds for distribution through our retail partners. Our retail partner beds have different model names, but have similar features and benefits, and sell for similar prices.

Each of our Sleep Number beds (not including our Precision Comfort adjustable foundation) comes with a 30 night in-home trial and better night’s sleep guarantee, which allows customers 30 nights at home to make sure they are completely satisfied with the bed. The customer is responsible for the return shipping costs. Independent durability testing has shown our Sleep Number beds can withstand more than 20 years of simulated use, and each of our Sleep Number beds is backed by our 20-year limited warranty.

Accessories and Other Products

In addition to our mattresses and foundations, we offer a line of accessory bedding products, including specialty pillows, mattress pads, comforters, sheets, bed foundations and leg options. The specialty pillows, available in a variety of sizes, materials and firmness levels, are designed to provide personalized comfort and better quality sleep for stomach, back or side sleepers. We also market our Personal Warmth Collection™, a group of comforters and blankets designed to be warmer on one half of the bed than the other, accommodating varying warmth preferences among couples.

In 2003, we completed the roll-out of our Precision Comfort adjustable foundation to all of our company-owned retail stores. The adjustable foundation enables consumers to raise the head or foot of the bed, and to experience the comfort of massage, using a handheld remote control.

Sales Distribution

Unlike traditional bedding manufacturers, which primarily sell through third-party retailers, over 90% of our net sales are through one of three company-controlled distribution channels – Retail, Direct Marketing and E-Commerce. These channels enable us to control the selling process to ensure that the unique benefits of our products are effectively presented to consumers. Our direct-to-consumer business model enables us to understand and respond quickly to consumer trends and preferences.

Our retail stores accounted for 78% of our net sales in 2008. Average net sales per company-owned store were $984,000 in 2008 versus $1,318,000 in 2007 and $626,000 in 2001, with average sales per square foot of $703 in 2008 versus $1,024 in 2007 and $666 in 2001. In 2008, 45% of our stores generated net sales of over $1,000,000.

Our direct marketing call center and E-Commerce Web site provide national sales coverage, including markets not yet served by one of our retail stores, and accounted for 14% of our net sales in 2008. In addition, these channels provide a cost-effective way to market our products, are a source of information on our products and refer customers to our stores if there is one near the customer.

Beginning in 2002, we supplemented our sales through semi-exclusive relationships with selected home furnishing retailers and specialty bedding retailers. At the end of 2008, our retail program included six retail partners in the U.S. and Canada with a total of 801 doors. Each retail partner serves a unique geographic market, which enables us to increase sales and leverage our media spending to accelerate brand awareness.

In late 2007, we began distribution in Australia and New Zealand through relationships with an Australian-based manufacturer and an Australian-based retailer. Our total net sales attributable to foreign countries were $5.4 million in 2008, $5.0 million in 2007 and $3.4 million in 2006.

Marketing and Advertising

Awareness among the broad consumer audience of our brand, product benefits and store locations has been our most significant opportunity for growth. The Sleep Number advertising campaign was introduced early in 2001 to support our retail stores in selected markets through our first comprehensive multi-media advertising campaign using prime-time TV, national cable television, infomercials, drive-time radio and newspaper advertisements.

Since 2001, the Sleep Number brand positioning has been integrated into our marketing messages across all of our distribution channels, advertising vehicles and media types. We look to our direct response advertising on national cable TV as an economical means to generate leads for our stores. Through our dedicated call center, we are able to provide the inquiring consumer more information or send a video and brochure. Our total media spending was approximately $92 million in 2008, $110 million in 2007 and $105 million in 2006.

Owners of Sleep Number beds purchased through company-controlled channels are members of our Comfort Club, our customer loyalty program designed primarily to increase referrals and repeat purchases. Each time a referred customer purchases a bed, the referring Comfort Club member receives a $50 coupon for purchase of our products, with increasing benefits for multiple referrals. In 2008, approximately 26,000 new customers bought beds after receiving referrals from our Comfort Club members, and existing owners bought approximately 30,000 additional beds.

Qualified customers are offered revolving credit to finance purchases through a private-label consumer credit facility provided by GE Money Bank. Approximately 37% of our net sales during 2008 were financed by GE Money Bank. In 2005, we entered into an amended and restated agreement with GE Money Bank that extends this consumer credit arrangement through February 15, 2011, subject to earlier termination upon certain events and subject to automatic extensions. Under the terms of our agreement, GE Money Bank sets the minimum acceptable credit ratings, the interest rates, fees and all other terms and conditions of the customer accounts, including collection policies and procedures, and is the owner of the accounts. In connection with all purchases financed under these arrangements, GE Money Bank pays us an amount equal to the total amount of such purchases, net of promotional related discounts, upon delivery to the customer. Consumers that do not qualify for credit under our agreement with GE Money Bank may apply for credit under a secondary program maintained by the company through another provider.

Operations

Manufacturing and Distribution

We have two manufacturing plants, one located in Irmo, South Carolina, and the other in Salt Lake City, Utah, which distribute products in the U.S. and Canada. The manufacturing operations in South Carolina and Utah consist of quilting and sewing of the fabric covers for our beds and final assembly and packaging of mattresses and foundations. In addition, our electrical Firmness Control Systems are assembled in our Utah plant.

We manufacture beds on a just-in-time basis to fulfill orders rather than stocking inventory, which enables us to maintain lower levels of finished goods inventory and operate with limited regional warehousing. Orders are shipped, typically within 48 hours following order receipt, from our manufacturing facilities via UPS or through our company-controlled home delivery, assembly and mattress removal service. Orders are usually received by the customer within five to 14 days from the date of order.

We obtain all of the raw materials and components used to produce our beds from outside sources. A number of components, including our proprietary air chambers, our proprietary blow-molded foundations, and various components for our Firmness Control Systems, as well as fabrics and zippers, are sourced from suppliers who currently serve as our sole source of supply for these components. Beginning in 2005, we initiated work on dual and alternate sourcing, successfully introducing a second source for printed circuit boards and certain foam and fiber components. We will continue working toward dual sourcing on

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targeted components. However, we believe we can obtain these raw materials and components from other sources of supply in the ordinary course of business, if necessary.

Our proprietary air chambers are produced to our specifications by a sole source Eastern European supplier, which has been our sole source of supply of air chambers since 1994. Our agreement with this supplier runs through September 2011 and is thereafter subject to automatic annual renewal unless either party gives 365 days' notice of its intention not to renew the agreement. We expect to continue this supplier relationship for the foreseeable future.

Our proprietary blow-molded foundations are produced to our specifications by a single domestic supplier under an agreement that expires in December 2012. We expect to continue this supplier relationship for the foreseeable future.

All of the suppliers that produce unique or proprietary products for us have in place either contingency or disaster recovery plans or redundant production capabilities in other locations in order to safeguard against any unforeseen disasters. We review these plans and sites on a regular basis to ensure the supplier's ability to maintain an uninterrupted supply of materials and components.

Home Delivery Service

Select Comfort's home delivery, assembly and mattress removal service has contributed to improving the overall customer experience. Our home delivery technicians typically are Sleep Number bed owners who can articulate the benefits of the bed, reinforcing the sales process and ensuring satisfied customers. Approximately 53% of beds sold through our company-owned retail stores in 2008 were delivered by our full-service home delivery team.

In 2003, we expanded the availability of our company-controlled delivery, assembly and removal services to all of our retail markets. In 2007, we continued improving our home delivery efficiency and service by consolidating over 100 individually managed cross-dock distribution locations into a Hub and Spoke network organized around 13 regional hubs.

Customer Service

We maintain an in-house customer service department staffed by customer service representatives who receive extensive training in sleep technology and all aspects of our products and operations. Our customer service representatives field customer calls and also interact with each of our retail stores to address customer questions and concerns. Our customer service team is part of our total quality process, facilitating early identification of emerging trends or issues. They coordinate with engineering, sourcing, manufacturing, and our Six Sigma team to segment these issues, implement immediate solutions and provide inputs for long-term improvements to product and service design.

Research and Development

Our research and development team continuously seeks to improve product performance and benefits based on sleep science. Through customer surveys and consumer focus groups, we seek feedback on a regular basis to help enhance our products. Since the introduction of our first bed, we have continued to improve and expand our product line, including new bed models, a quieter Firmness Control System, wireless remote controls, more luxurious fabrics and covers, and new generations of foams and foundation systems. Our research and development expenses were $3.4 million in 2008, $5.7 million in 2007 and $4.7 million in 2006.

Information Systems

We use information technology systems to operate, analyze and manage our business, to reduce operating costs and to enhance our customers' experience. Our major systems include an in-store point of sale system, a retail portal system, in-bound and out-bound telecommunications systems for direct marketing and customer service, E-Commerce systems, a data warehouse system and an enterprise resource planning system. These systems are comprised of both packaged applications licensed from various software vendors and internally developed programs. Our production data center and E-Commerce Web site is located in our new state-of-the-art corporate headquarters with redundant environmental systems. We maintain a disaster recovery plan that is tested regularly.

During the fourth quarter of fiscal 2008, we abandoned our plan to implement an integrated suite of SAP®-based applications in 2009. Our plan in the short-term is to maintain our existing information systems capabilities to effectively operate, analyze and manage our business.

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Intellectual Property

We hold various U.S. and foreign patents and patent applications regarding certain elements of the design and function of our products, including air control systems, remote control systems, air chamber features, border wall and corner piece systems, foundation systems, and features related to sofa sleepers with air mattresses, as well as other technology. We have 24 issued U.S. patents, expiring at various dates between March 2009 and June 2022, and five U.S. patent applications pending. We also hold 31 foreign patents and 9 foreign patent applications pending. Notwithstanding these patents and patent applications, we cannot ensure that these patent rights will provide substantial protection or that others will not be able to develop products that are similar to or competitive with our products. To our knowledge, no third party has asserted a claim against us alleging that any element of our product infringes or otherwise violates any intellectual property rights of any third party.

"*Select Comfort*" and "*Sleep Number*" are trademarks registered with the U.S. Patent and Trademark Office. We have a number of other registered trademarks including our "*Select Comfort*" logo with the double arrow design, "*Select Comfort Creator of the Sleep Number Bed*," "*What's Your Sleep Number?*," "*Precision Comfort*," "*The Sleep Number Bed by Select Comfort*" (logo), "*The Sleep Number Store by Select Comfort*" (logo), "*Comfort Club*" and "*Sleep Better on Air*" and "*LuxLayer*." U.S. applications are pending for a number of other marks. Several of these trademarks have been registered, or are the subject of pending applications, in various foreign countries. Each federally registered mark is renewable indefinitely as long as the mark remains in use. We are not aware of any material claims of infringement or other challenges asserted against our right to use these marks.

Industry and Competition

The U.S. bedding manufacturing industry is a mature and generally stable industry. According to the International Sleep Products Association (ISPA), since 1984 the industry has consistently demonstrated growth on a dollar basis, with a 0.3% decline in 2001 and 11.9% decline in 2008 being the only exceptions. According to ISPA, industry wholesale shipments of mattresses and foundations were estimated to be $6.1 billion in 2008, an 11.9% decline compared to $6.9 billion in 2007. We estimate that traditional innerspring mattresses represent approximately 75% of total U.S. bedding sales. *Furniture/Today*, a furniture industry trade publication, has ranked Select Comfort as the largest U.S. bedding retailer for seven consecutive years, most recently in its August 11, 2008 issue.

Over the 5-year, 10-year and 20-year periods ended 2008, the value of U.S. wholesale bedding shipments increased at compound annual growth rates of 3.2%, 4.2% and 5.0%, respectively. We believe that industry unit growth has been primarily driven by population growth, and an increase in the number of homes (including secondary residences) and the increased size of homes. We believe growth in average wholesale prices resulted from a shift to both larger and higher quality beds, which are typically more expensive.

The bedding industry is highly fragmented and very competitive. Participants in the bedding industry compete primarily on price, quality, brand name recognition, product availability and product performance, including the perceived levels of comfort and support provided by a mattress. There is a high degree of concentration among the three largest manufacturers of innerspring bedding with nationally recognized brand names, including Sealy, which also owns the Stearns & Foster brand name, Serta, and Simmons. Numerous other manufacturers, primarily operating on a regional or niche basis, serve the balance of the bedding market. Simmons and Sealy, as well as a number of smaller manufacturers, have offered air-bed products in recent years. Tempur-Pedic International, Inc., and a number of other mattress manufacturers, offer foam mattress products.

Governmental Regulation and Environmental Matters

Our operations are subject to federal and state consumer protection and other regulations relating to the bedding industry. These regulations vary among the jurisdictions in which we do business, but generally impose requirements as to the proper labeling of bedding merchandise.

A portion of our net sales consists of refurbished products that are assembled in part from components returned to us from customers. These refurbished products must be properly labeled and marketed as refurbished products under applicable laws. Our sales of refurbished products are limited to approximately 24 states, as other states do not allow the sale of refurbished bedding products or have more stringent requirements that we choose not to follow.

The bedding industry is subject to federal fire retardancy standards developed by the U.S. Consumer Product Safety Commission, which became effective nationwide in July 2007. Compliance with these requirements has increased the cost

and complexity of manufacturing our products, potentially reducing our manufacturing capacity. These regulations also result in higher product development costs as new products must undergo rigorous flammability testing.

The Consumer Product Safety Commission has also adopted, effective as of February 2009, new safety standards applicable to children's products generally, including some mattress products. Compliance with these standards may increase the cost of manufacturing some of our products.

Our direct marketing and E-Commerce operations are or may become subject to various adopted or proposed federal and state "do not call" and "do not mail" list requirements, limiting our ability to market our products directly to consumers over the telephone, by e-mail or by regular mail.

We are subject to emerging federal, state and foreign data privacy regulations related to the safeguarding of sensitive customer and employee data, which may limit our ability to maintain or use consumer or customer information in our business.

We are subject to federal, state and foreign labor laws, including but not limited to laws relating to occupational health and safety, employee privacy, wages and hours, overtime pay, harassment and discrimination, equal opportunity, and employee leaves and benefits.

We are subject to federal and state laws and regulations relating to pollution and environmental protection. We will also be subject to similar laws in foreign jurisdictions as we further expand distribution of our products internationally.

Our retail pricing policies and practices are subject to antitrust regulations in the U.S., Canada, Australia, New Zealand and other jurisdictions where we may sell our products in the future.

Although we believe that we are in compliance in all material respects with these regulations and have implemented a variety of measures to promote continuing compliance, regulations may change over time and we may be required to incur expenses and/or to modify our operations in order to ensure compliance with these regulations, which could harm our profitability and financial condition. If we are found to be in violation of any of the foregoing laws or regulations, we could become subject to fines, penalties, damages or other sanctions, as well as potential adverse public relations, which could adversely impact our business, reputation, sales, profitability and financial condition.

We are not aware of any national or local provisions which have been enacted regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, that have materially affected, or will materially affect, our net income or competitive position, or will result in material capital expenditures. During fiscal 2008, there were no material capital expenditures for environmental control facilities and no such material expenditures are anticipated.

Customers

No single customer accounts for 10% or more of our net sales. The loss of distribution through QVC, however, could adversely impact our sales, profitability and financial condition.

Seasonality

Our business is modestly impacted by seasonal influences inherent in the U.S. bedding industry and general retail shopping patterns. The U.S. bedding industry generally experiences lower sales in the second quarter and increased sales during selected holiday or promotional periods.

Working Capital

The component nature of our products allows our stores to serve as product showrooms for our Sleep Number beds. This aspect of our business model allows us to maintain low inventory levels which enables us to operate with minimal working capital. We have historically generated sufficient cash flows to self-fund operations through an accelerated cash-conversion cycle. However, the 2008 decline in our operating performance has significantly affected our ongoing liquidity. As of January 3, 2009, we had outstanding borrowings of $79.2 million, plus $5.9 million under letters of credit, with an additional $5.0 million available under our $90 million credit facility. Pursuant to a series of amendments of our Credit Agreement, the Lenders have deferred to March 31, 2009 a reduction in the amount available under our line of credit from $90 million to $85 million that was previously scheduled to become effective as of December 1, 2008. Also pursuant to these amendments, the Lenders have waived compliance, through the close of business on March 30, 2009, with certain financial covenants under the

Credit Agreement applicable to fiscal periods ending on or about December 31, 2008, January 31, 2009 and February 28, 2009. Upon expiration of our most recent amendment on March 31, 2009, we will not be in compliance with certain financial covenants under the Credit Agreement. If we are unable to continue to obtain amendments from the Lenders that waive compliance with these financial covenants, the Lenders could place us in default under the terms of the Credit Agreement. In early March 2009, we received a federal income tax refund of approximately $23.0 million. Pursuant to the terms of the Credit Agreement, these funds have been placed in a cash collateral account with the Lenders. We are in discussions with the Lenders regarding the potential use or application of these funds to address our near-term liquidity needs.

We have been exploring a range of strategic and financing alternatives to enhance our financial flexibility. If we are unable to obtain additional capital, we may not be able to fund our operating needs and we could face a risk of default under our Credit Agreement.

Employees

At January 3, 2009, we employed 2,571 persons, including 1,509 retail sales and support employees, 190 direct marketing and customer service employees, 633 manufacturing and logistics employees, and 239 management and administrative employees. Approximately 158 of our employees were employed on a part-time basis at January 3, 2009. Except for managerial employees and professional support staff, all of our employees are paid on an hourly basis plus commissions for sales associates. None of our employees are represented by a labor union or covered by a collective bargaining agreement. We believe that our relations with our employees are good.

Executive Officers of the Registrant

William R. McLaughlin, 52, joined our company in March 2000 as President and Chief Executive Officer. Mr. McLaughlin also served as Chairman of our Board of Directors from May 2004 to February 2008. From December 1988 to March 2000, Mr. McLaughlin served as an executive of PepsiCo Foods International, Inc., a snack food company and subsidiary of PepsiCo, Inc., in various capacities, including from September 1996 to March 2000 as President of Frito-Lay Europe, Middle East and Africa, and from June 1993 to June 1996 as President of Grupo Gamesa, S.A. de C.V., a cookie and flour company based in Mexico.

Shelly R. Ibach, 49, has served as Executive Vice President, U.S. Sales since October 2008. Ms. Ibach joined Select Comfort as Senior Vice President, U.S. Sales - Company Owned Channels in April 2007. From 1982 to 2007, she held various leadership positions within Macy's North, formerly Marshall Field's Department Stores - Target Corporation. From 2004 to 2007, Ms. Ibach served as Senior Vice President and General Merchandise Manager for the Home division, within Macy's North. Other key positions included Vice President - Divisional Merchandise Manager, Director of Planning and Regional Director of Stores.

Mark A. Kimball, 50, has served as Senior Vice President, Legal, General Counsel and Secretary since August 2003. From July 2000 to August 2003, Mr. Kimball served as Senior Vice President, Human Resources and Legal, General Counsel and Secretary. From May 1999 to July 2000, Mr. Kimball served as our Senior Vice President, Chief Administrative Officer, General Counsel and Secretary. For more than five years prior to joining us, Mr. Kimball was a partner in the law firm of Oppenheimer Wolff & Donnelly LLP practicing in the area of corporate finance.

James C. Raabe, 49, has served as Senior Vice President and Chief Financial Officer since April 1999. From September 1997 to April 1999, Mr. Raabe served as our Controller. From May 1992 to September 1997, he served as Vice President – Finance of ValueRx, Inc., a pharmacy benefit management provider. Mr. Raabe held various positions with KPMG LLP from August 1982 to May 1992.

Karen R. Richard, 38, has served as VP, Chief Human Resource & Strategy Officer for Select Comfort Corporation since December 2008. From January 2006 through July 2008, Ms. Richard served as Vice President, Human Resources and prior to that she served as Vice President, Finance supporting Select Comfort's Consumer Channels and Marketing. Ms. Richard also held a variety of positions in the company's finance department after joining Select Comfort in May of 1996. From 1993 to 1996, Ms. Richard held various accounting positions with TCF Mortgage Corporation, an affiliate of TCF Financial Corporation.

Kathryn V. Roedel, 48, has served as Executive Vice President, Product Development and Operations since October 2008. Ms. Roedel joined our Company as Senior Vice President, Global Supply Chain in April 2005. From 1983 to 2005, she held leadership positions within two divisions of General Electric Company, in Sourcing, Manufacturing, Quality and Service. From 2003 to March 2005, Ms. Roedel served as the General Manager, Global Supply Chain Strategy for GE Medical Systems. Other key positions included General Manager, Global Quality and Six Sigma; Vice President – Technical Operations and Director/Vice President – Quality Programs for GE Clinical Services, a division of GE Medical Systems.

Wendy L. Schoppert, 42, joined our company as Senior Vice President and General Manager – New Channel Development & Strategy in April 2005 and effective January 2007, became our Senior Vice President – International. In March 2008, Ms. Schoppert also assumed the responsibilities of Chief Information Officer for the company. From 2002 to March 2005,

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Ms. Schoppert led various departments within U.S. Bancorp Asset Management, most recently serving as Head of Private Asset Management and Marketing. From 1996 to 2000, she held several positions with America West Holdings Corporation, including Vice President of America West Vacations and head of the airline's Reservations division. Prior to 1996, Ms. Schoppert held various finance-related positions at both Northwest Airlines and American Airlines.

Tim Werner, 45, has served as Vice President and Chief Marketing Officer since March 2009. From October 2008 through February 2009 he served as Vice President, Marketing. Mr. Werner served as Vice President, Direct and E-Commerce from October 2007 to September 2008 and as Vice President, Retail Partners developing our Wholesale business from October 2002 to July 2006. Mr. Werner also held a variety of positions in our Direct channel business after joining us in May 1996. From 1986 to 1996, Mr. Werner held marketing positions with L.L. Bean, Inc. and Fingerhut Corporation.

Available Information

We are subject to the reporting requirements of the Exchange Act and its rules and regulations. The Exchange Act requires us to file reports, proxy statements and other information with the Securities and Exchange Commission ("SEC"). Copies of our reports, proxy statements and other information can be read and copied at:

SEC Public Reference Room
100 F Street NE
Washington, D.C. 20549

Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains a Web site that contains reports, proxy statements and other information regarding issuers that file electronically with the SEC. These materials may be obtained electronically by accessing the SEC's home page at *http://www.sec.gov*.

Our corporate Internet Web site is *http://www.selectcomfort.com*. Through a link to a third-party content provider, our corporate Web site provides free access to our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after electronic filing with the SEC. These documents are posted on our Web site at *www.selectcomfort.com* — select the "*About Select Comfort*" link and then the "*Investor Relations*" link. The information contained on our Web site or connected to our Web site is not incorporated by reference into this Form 10-K and should not be considered part of this report.

We also make available, free of charge on our Web site, the charters of the Audit Committee, Management Development and Compensation Committee, Corporate Governance and Nominating Committee and Finance Committee as well as our Code of Business Conduct (including any amendment to, or waiver from, a provision of our Code of Business Conduct) adopted by our Board. These documents are posted on our Web site — select the "*Investor Relations*" link and then the "*Corporate Governance*" link.

Copies of any of the above referenced information will also be made available, free of charge, upon written request to:

Select Comfort Corporation
Investor Relations Department
9800 59th Avenue North
Minneapolis, MN 55442

ITEM 1A. RISK FACTORS

Liquidity and Capital Resources and Our Ability to Continue as a Going Concern. We may not have adequate liquidity and capital resources to fund our operating needs and continue as a going concern. We are seeking to raise additional capital through the issuance of debt or equity securities or a combination thereof, which may adversely impact our profitability and may be substantially dilutive to our existing shareholders. If we are unable to obtain additional capital, we may not be able to fund our operating needs, we would face a risk of default under our Credit Agreement and we may not be able to continue as a going concern. Our uncertain financial position may also disrupt relationships with our suppliers and adversely impact our sales.

As of January 3, 2009, we had cash and cash equivalents of $13.1 million and $79.2 million in outstanding borrowings, plus $5.9 million under letters of credit, against our $90 million line of credit. Cash generated from operations and remaining funds available under our existing credit facility may not provide sufficient liquidity for our operating and capital needs. Pursuant to a series of amendments of our Credit Agreement, the Lenders have deferred to March 31, 2009 a reduction in the amount available under our line of credit from $90 million to $85 million that was previously scheduled to become effective as of December 1, 2008. Also pursuant to these amendments, the Lenders have waived compliance, through the close of business on March 30, 2009, with certain financial covenants under the Credit Agreement applicable to fiscal periods ending on or about December 31, 2008, January 31, 2009 and February 28, 2009. In early March 2009, we received a federal income tax refund of approximately $23.0 million. Pursuant to the terms of the Credit Agreement, these funds have been placed in a cash collateral account with the Lenders. We are in discussions with the Lenders regarding the potential use or application of these funds to address our near-term liquidity needs.

Our independent public accounting firm has issued an opinion on our consolidated financial statements stating that the consolidated financial statements have been prepared assuming we will continue as a going concern. The opinion further states that our losses from operations and inability to generate sufficient cash flow to meet obligations and sustain operations raise substantial doubt about our ability to continue as a going concern. This opinion, as well as our uncertain financial position, may disrupt relationships with our suppliers, which may prevent us from obtaining necessary components, supplies or services on acceptable terms or at all, and may adversely impact consumer confidence in our ability to honor our warranty obligations, which may adversely impact our sales, profitability and financial condition.

We are seeking to raise additional capital through the issuance of debt or equity securities and to restructure the credit facility under the Credit Agreement in order to provide adequate financial flexibility and liquidity to fund our operations and to avoid default under the Credit Agreement. The issuance of any additional debt securities or the restructuring of our credit facility could materially and adversely impact our profitability through higher interest costs and other fees. The issuance of additional equity securities could be substantially dilutive to our existing shareholders.

If we are unable to obtain additional capital, we may not be able to finance our operating needs and the Lenders under the Credit Agreement may not continue to defer the reduction in availability under the line of credit or continue to waive compliance with prior or future financial covenants, which may result in a default under the Credit Agreement. A default under the Credit Agreement would enable the Lenders to seek immediate payment in full of any amounts outstanding under the credit facility and to exercise various remedies as secured creditors, which may severely or completely constrain our ability to continue to operate our business as a going concern and may require us to seek protection from creditors through bankruptcy proceedings.

Uncertainty of Future Growth and Profitability. Our future growth and profitability will depend on a number of factors.

After more than five consecutive years of growth in both sales and profitability through fiscal 2006, our sales and profitability declined in 2008 and 2007 versus the prior years. We may not be able to regain growth in sales or improvement in profitability on a quarterly or annual basis in future periods. Our future growth and profitability will be impacted by or dependent upon a number of factors, including but not limited to:

- *Liquidity and Capital Resources* -- our ability to obtain and maintain adequate liquidity and capital resources to fund our operating and capital needs, including our ability to remain in compliance with the financial covenants and other requirements under our credit agreement;
- *General Economic Conditions and Consumer Confidence* -- adverse trends in general economic conditions, including in particular adverse trends in the housing market, retail shopping patterns, consumer confidence and credit markets, the uncertainty of the depth and duration of the current economic recession and the uncertainty of the timing and strength of any economic recovery;

- *Marketing Effectiveness and Efficiency* -- the effectiveness of our marketing messages and the efficiency of our advertising expenditures and other marketing programs in building product and brand awareness, driving traffic to our points of sale and increasing sales;
- *Consumer Acceptance* -- the level of consumer acceptance of our products, new product offerings and brand image;

- *Consumer Credit* -- the availability of consumer credit and our ability to provide cost-effective consumer credit options, particularly in light of the current challenges in the consumer credit market; in the event that one or both of our providers of consumer credit determine to impose more stringent credit requirements or terms, our sales could be adversely impacted;

- *Execution of Our Retail Distribution Strategy* -- our ability to execute our retail store distribution strategy in the current economic environment, including increasing sales and profitability through our existing stores and cost-effectively closing under-performing store locations;

- *Sources of Materials and Services* -- our ability to secure adequate sources of necessary materials and services at reasonable cost, especially considering our uncertain financial position, our single sources of supply for some components and services, our just-in-time manufacturing processes, potential shortages of commodities, and the macroeconomic environment, which may place financial pressures on our suppliers;

- *Inflationary Pressures* -- rising fuel and commodity costs, as well as fluctuating currency rates and increasing industry regulatory requirements, which may increase our cost of goods and may adversely impact our profitability or our ability to maintain sales volumes to the extent that we choose to increase prices;

- *Competition* -- the level of competition in the mattress industry and our ability to successfully identify and respond to emerging and competitive trends in the mattress industry;

- *Need for Continuous Product Improvement* -- our ability to continuously improve our products to offer new and enhanced consumer benefits, better quality and reduced costs;

- *Impact of Federal Flammability Standards* -- new federal flammability standards for mattress products effective since mid-2007, which have added compliance and product costs to our business and have added risks of non-compliance, which could disrupt our business;

- *Impact of Federal Safety Standards* -- new federal safety standards for children's products, including some mattress products, effective in February 2009, which may add compliance and product costs to our business and have added risks of non-compliance, which could disrupt our business;

- *Management Information Systems* -- the adequacy of our current management information systems, and our ability to maintain and enhance our management information systems, to meet the evolving requirements of our business and regulatory standards, including evolving payment card industry and federal and state regulatory standards applicable to data privacy and security;

- *Retention of Senior Leadership and other Key Employees* -- our ability to retain senior leadership and other key employees, including qualified retail store management and sales professionals, in the wake of recent business performance that has not met our expectations;

- *International Growth* -- our ability to cost-effectively manage and expand our distribution in Canada, Australia and New Zealand; and

- *Global Events* -- global events, such as terrorist attacks or a pandemic outbreak, or the threat of such events.

We may not be successful in executing our growth strategy or in regaining growth in sales or improvement in profitability. Failure to successfully execute any material part of our strategic plan or growth strategy could harm our sales, profitability and financial condition.

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Dependence on General Economic Conditions and Consumer Spending. We are highly dependent on discretionary consumer spending. Adverse trends in general economic conditions, including in particular the housing market, retail shopping patterns, consumer confidence, credit markets and employment levels, may continue to adversely affect our sales, profitability and financial condition.

The success of our business models depends to a significant extent upon discretionary consumer spending, which is subject to a number of factors, including without limitation general economic conditions, consumer confidence, the housing market, employment levels, business conditions, interest rates, availability of credit, inflation and taxation. Adverse trends in any of these economic indicators may adversely affect our sales, profitability and financial condition. Also, because a high percentage of our net sales are made on credit, any adverse impact on the availability of consumer credit or any increase in interest rates may adversely affect our sales, profitability and financial condition. We are also dependent upon the continued popularity of malls as shopping destinations and the ability of mall anchor tenants and other attractions to generate customer traffic for our retail stores. Any decrease in mall traffic could adversely affect our sales, profitability and financial condition.

Effectiveness and Efficiency of Marketing and Advertising. Our future growth and profitability will depend in large part upon the effectiveness of our marketing messages and the efficiency of our advertising expenditures and other marketing programs in generating consumer awareness and sales of our products.

We are highly dependent on the effectiveness of our marketing messages and the efficiency of our advertising expenditures (which were approximately $92 million in 2008, $110 million in 2007, $105 million in 2006, $89 million in 2005, and $79 million in 2004) in generating consumer awareness and sales of our products. In recent periods, including in particular 2007 and 2008, our marketing messages have not been as effective as in prior periods. If our marketing messages are ineffective or our advertising expenditures and other marketing programs are inefficient in creating awareness of our products and brand name, driving consumer traffic to our points of distribution and motivating consumers to purchase our products, our sales, profitability and financial condition may be adversely impacted.

We plan to significantly reduce our advertising expenditures in 2009 in comparison with prior periods, which may adversely impact our sales, profitability and financial condition.

Our integrated marketing program depends in part on national radio personalities and spokespersons and other nationally known personalities. The loss of these endorsements, or any reduction in the effectiveness of these endorsements, or our inability to obtain additional effective endorsements, could adversely affect our sales, profitability and financial condition.

Dependence on Internet Marketing Programs. Our future growth and profitability will depend in part upon the effectiveness and efficiency of our internet-based advertising programs and upon the prominence of our Web site URLs on internet search engine results.

We believe that consumers are increasingly using the internet as a part of their shopping experience, both to conduct pre-purchase research, particularly with respect to high-end consumer durables, as well as to purchase products. Consumers will typically use one of a small number of internet search engines to research products. These search engines may provide both natural search results and purchased listings for particular key words. In some cases, it may be difficult or impossible to determine how these search engines work, particularly in the area of natural search, and therefore how to optimize placement on those search engines for our Web site URLs and other positive sites for consumers who may be searching for our products or for mattress products or retailers generally. Some of these search engines may permit competitors to bid on our trademarks to obtain high placement in search results when consumers use our trademarks to seek information regarding our products, which may cause confusion among consumers and adversely impact our sales. Some of our competitors may use our trademarks and/or publish false or misleading information on the internet regarding our products or their own products, which may also cause confusion among consumers and adversely impact our sales. In addition, consumers or others may post negative information regarding our products or our company on internet sites or blogs, which could adversely impact our sales.

As a result, our future growth and profitability will depend in part upon the effectiveness and efficiency of our on-line advertising and search optimization programs in generating consumer awareness and sales of our products, and upon our ability to prevent competitors from misusing or infringing our trademarks or publishing false or misleading information regarding our products or their own products. If we are not successful in these efforts, our business, reputation, sales, profitability and financial condition may be adversely impacted.

In addition, if our Web site becomes unavailable for a significant period of time due to failure of our information technology systems or the Internet, our sales, profitability and financial condition could be adversely affected.

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Uncertainty of Consumer Acceptance. Our products represent a significant departure from traditional innerspring mattresses and the failure of our products to achieve market acceptance would harm our sales, profitability and financial condition.

We estimate that innerspring mattress sales represent approximately 75% or more of all mattress sales. Our air chamber technology represents a significant departure from traditional innerspring mattresses. Because no established market for adjustable firmness mattress products existed prior to the introduction of our products in 1988, we faced the challenge of establishing the viability of this market, as well as gaining widespread acceptance of our products. The market for adjustable firmness mattresses is now evolving and our future success will depend upon both the continued growth of this market and increased consumer acceptance of our products. The failure of our products to achieve greater consumer acceptance for any reason would harm our sales, profitability and financial condition.

Dependence on Availability of Consumer Credit. More than one-third of our net sales are financed under a consumer credit program provided by a third party. The termination of this consumer credit program, any material change to the terms of this consumer credit program or in the availability or terms of credit offered to our customers under this consumer credit program, or any delay in securing replacement credit sources, could harm our sales, profitability and financial condition.

In December 2005 we entered into an amended and restated agreement under which GE Money Bank offers our qualified customers a revolving credit arrangement to finance purchases from us. This agreement extends through February 15, 2011, subject to earlier termination upon certain events and subject to automatic extensions.

Under this agreement, GE Money Bank sets the minimum acceptable credit ratings, the interest rates, fees and all other terms and conditions of the customer accounts, including collection policies and procedures, and is the owner of the accounts. Any increase by GE Money Bank in the minimum customer credit ratings necessary to qualify for credit could adversely impact our sales by decreasing the number of customers who can finance purchases. We are liable to GE Money Bank for charge-backs arising out of (i) breach of our warranties relating to the underlying sale transaction, (ii) defective products or (iii) our failure to comply with applicable operating procedures under the facility. We are not liable to GE Money Bank for losses arising out of our customers' credit defaults.

Our agreement with GE Money bank contains certain financial covenants, including a maximum leverage ratio and a minimum interest coverage ratio. As our recent results placed us outside of these financial covenants, we were required under the terms of the agreement to provide GE money Bank with a $2.7 million letter of credit as collateral security.

Approximately 37% of our net sales during 2008 were financed by GE Money Bank. Consumers that do not qualify for credit under our agreement with GE Money Bank may apply for credit under a secondary program maintained by the company through another provider.

Termination of our agreement with GE Money Bank or with our secondary provider, any material change to the terms of our agreement with either of these providers, or in the availability or terms of credit for our customers from these providers, or any delay in securing replacement credit sources, could harm our sales, profitability and financial condition.

Risks of Retail Store Distribution Strategy. Our future growth and profitability will depend in large part upon our ability to execute our retail store distribution strategy, including increasing sales and profitability through our existing company-controlled stores, which carry significant fixed costs, and cost-effectively closing under-performing stores. If we are unable to regain growth in sales through our company-controlled stores, we may be required to incur significant costs to close underperforming stores, which could harm our profitability and financial condition.

Our company-controlled retail store distribution channel is our largest distribution channel and represents our largest opportunity for growth in sales and improvement in profitability. After several years of consistent growth in comparable store sales results through fiscal 2006, in 2007 we experienced a *decline* of 11% in our comparable stores sales versus 2006, and in 2008 we experienced a further decline of 25% in our comparable store sales versus 2007. After achieving profitability in the third quarter of 2008, our comparable store sales results declined by 29% in the fourth quarter of 2008 in comparison to fourth quarter of 2007. Our comparable-store sales and other operating results may fluctuate or decline significantly in the future. Many factors affect our comparable-store sales and other operating results and may contribute to fluctuations or declines in these results in the future, including but not limited to:

- The effectiveness of our marketing messages and the efficiency of our advertising expenditures;

- Consumer acceptance of our existing products, new product offerings and brand image;
- Consumer shopping trends, including mall traffic and internet shopping trends, and the increasing availability of retail shopping venues other than traditional retail malls;
- Our ability to successfully hire, train, motivate and retain store-level sales professionals and managers;
- The level and effectiveness of competitive activity;
- The availability of cost-effective consumer credit options through our third-party providers;
- The growth of our other distribution channels, including in particular the wholesale distribution of our products through mattress retailers into markets with existing company-controlled retail stores;
- General economic conditions, including in particular the housing market, retail trends and consumer confidence; and
- Global events, such as terrorist attacks or a pandemic outbreak, or the threat of such events.

Future fluctuations or decreases in our comparable-store sales or other operating results could harm our sales, profitability and financial condition. We may also be required to incur significant costs to close underperforming stores if we are unable to regain growth in sales in under-performing stores. In addition, failure to regain growth in comparable-store sales or other operating results may disappoint securities analysts or investors and result in a decline in our stock price.

Risks of Wholesale Distribution Strategy. We have established wholesale relationships with a limited number of mattress retailers and with the QVC shopping channel. These relationships may not yield the benefits we expect and may adversely impact sales through our company-controlled distribution channels. The loss of a significant wholesale account or the loss of distribution through QVC could adversely impact our sales, profitability and financial condition.

An important element of our growth strategy has been expansion of profitable distribution through our existing company-controlled distribution channels and increasing opportunities for consumers to become aware of, and to purchase, our products through additional points of distribution. We have only limited experience with a small number of mattress retailers and with the QVC shopping channel, and these wholesale relationships may not yield the intended benefits of leveraging our advertising spending and increasing our brand awareness, sales and overall market acceptance of our products. Our wholesale distribution may also adversely impact sales through our company-controlled distribution channels. The gross margin from wholesale sales is also less than the gross margin we generate in our company-controlled channels. The loss of distribution through QVC could adversely impact our sales, profitability and financial condition.

Dependence on Key Suppliers. We rely upon several key suppliers that are, in some instances, the only source of supply currently used by the company for particular materials or components. The failure of one or more of these suppliers or our other key suppliers to supply materials or components for our products on a timely basis, or a material change in the purchase terms for the materials or components, could harm our sales, profitability and financial condition.

We currently obtain all of the materials and components used to produce our beds from outside sources. In several cases, including our proprietary air chambers, our proprietary blow-molded foundations, the wood foundations sold to our wholesale and hospitality channels, our adjustable foundations, various components for our Firmness Control Systems, as well as fabrics and zippers, we have chosen to obtain these materials and components from suppliers who serve as the only source of supply used by the company at this time. While we believe that these materials and components, or suitable replacements, could be obtained from other sources of supply, in the event that any of the company's current suppliers became unable to supply the relevant materials or components for any reason, and alternatives were not readily available from other sources of supply, our sales, profitability and financial condition could be harmed. If our relationship with either the supplier of our air chambers or the supplier of our blow-molded foundations is terminated, we could have difficulty in replacing these sources since there are relatively few other suppliers capable of manufacturing these components.

We purchase some of our materials and components through purchase orders and do not have long-term purchase agreements with, or other contractual assurances of continued supply, pricing or access from, our suppliers, except for the suppliers of

our air chambers, blow-molded foundations, foam, circuit boards and various components used for our covers, including fiber, fabrics, thread and tick. If prices for our key materials or components increase and we are unable to achieve offsetting savings through value engineering or increased productivity or we are unable to increase prices to our customers, our profitability and financial condition may be harmed. The loss of one or more of our key suppliers, the failure of one or more of our key suppliers to supply materials or components on a timely basis, or a material change in the purchase terms for our components could harm our sales, profitability and financial condition.

Our uncertain financial position may also disrupt relationships with our suppliers, which may prevent us from obtaining necessary components, supplies or services on acceptable terms or at all.

Inflationary Pressures. Increases in commodity prices, component costs and/or delivery costs could harm our sales, profitability and financial condition.

Recently there have been significant increases or volatility in the prices of certain commodities, including but not limited to fuel, oil, natural gas, rubber, cotton, plastic resin, steel and chemical ingredients used to produce foam. Increases in prices of these commodities may result in significant cost increases for our raw materials and product components, as well as increases in the cost of delivering our products to our customers. To the extent we are unable to offset any such increased costs through value engineering and similar initiatives underway, or through price increases, our profitability and financial condition may be adversely impacted. If we choose to increase prices to offset the increased costs, our unit sales volumes could be adversely impacted.

Risks of Just-In-Time Manufacturing Processes. We utilize "just-in-time" manufacturing processes with minimal levels of raw materials, work in process and finished goods inventories, which could leave us vulnerable to shortages of supply of key components. Any such shortage could result in our

inability to satisfy consumer demand for our products in a timely manner and lost sales, which could harm our sales, profitability and financial condition.

We generally assemble our products after we receive orders from customers utilizing “just-in-time” manufacturing processes. Lead times for ordered components may vary significantly and depend upon a variety of factors, such as the location of the supplier, the complexity in manufacturing the component and general demand for the component. Some of our components, including our air chambers, have relatively longer lead times. We generally maintain minimal levels of raw materials, work in process and finished goods inventories, except for our air chambers, of which we generally carry approximately six weeks of inventory. As a result, an unexpected shortage of supply of key components used to manufacture our products, or an unexpected and significant increase in the demand for our products, could lead to inadequate inventory and delays in shipping our beds to customers. Any such delays could result in lost sales, which could harm our profitability and financial condition.

Risks of Foreign Sourcing of Materials. The foreign manufacturing of our air chambers and some of our other components involves risks that could increase our costs, lead to inadequate inventory levels or delays in shipping beds to our customers, which could harm our sales, profitability and financial condition.

Since our air chambers and some of our other components are manufactured outside the United States, our operations could be harmed by the risks associated with foreign sourcing of materials, including but not limited to:

- Political instability resulting in disruption of trade;
- Existing or potential duties, tariffs or quotas that may limit the quantity of certain types of goods that may be imported into the United States or increase the cost of such goods;
- Disruptions in transportation that could be caused by a variety of factors including acts of terrorism, shipping delays, foreign or domestic dock strikes, customs inspections or other factors;
- Any significant fluctuation in the value of the U.S. dollar against foreign currencies; and
- Economic uncertainties, including inflation.

These factors could increase our costs of doing business with foreign suppliers, lead to inadequate inventory levels or delays in shipping beds to our customers, which could harm our sales, profitability and financial condition. If any of these or other factors were to render the conduct of any of our foreign suppliers’ businesses more difficult or impractical, we may have

difficulty sourcing key components of our products, which could adversely affect our sales, profitability and financial condition.

Dependence on UPS and Other Carriers. We depend upon UPS and other carriers to deliver some of our products to customers on a timely and cost-effective basis. Any significant delay in deliveries to our customers could lead to increased returns and cause us to lose sales. Any increase in freight charges could increase our costs of doing business and harm our sales, profitability and financial condition.

Historically, we have relied to a significant extent on UPS for delivery of our products to customers. For a significant portion of the third quarter of 1997, UPS was unable to deliver our products within acceptable time periods due to a labor strike, causing delays in deliveries to customers and requiring us to use alternative carriers. UPS may not be able to avert labor difficulties in the future or may otherwise experience difficulties in meeting our requirements in the future. From 2000 to 2003, we demonstrated an ability to shift a portion of our product delivery business to FedEx, as necessary. In addition, we either provide directly, or contract with a third party to provide, in-home delivery, assembly and mattress removal services, and in 2003 expanded the availability of this service to all of our retail stores across the country. Despite these alternative carriers, if UPS were to experience difficulties in meeting our requirements, we may not be able to deliver products to all of our customers on a timely or cost-effective basis through any alternative carriers. Any significant delay in deliveries to our customers could lead to increased returns and cause us to lose sales. Any increase in freight charges could increase our costs of doing business and harm our sales, profitability and financial condition.

Risk of Damage to our Manufacturing Facilities. Damage to either of our manufacturing facilities could increase our costs of doing business or lead to delays in shipping our beds, which could result in increased returns and adversely affect future sales.

We have two manufacturing plants, which are located in Irmo, South Carolina and in Salt Lake City, Utah. Unlike other mattress manufacturers, we generally manufacture beds to fulfill orders rather than stocking finished goods inventory. Therefore, the destruction or shutting down of either of our manufacturing facilities for a significant period of time as a result of fire, explosion, act of war or terrorism, flood, hurricane, tornado, earthquake, lightning or other natural disaster could increase our costs of doing business and lead to delays in shipping our beds to customers. Such delays could result in increased returns and adversely affect future sales, which could harm our profitability and financial condition. Due to our make-to-order business model, these adverse consequences to our business may be greater for our company than with other mattress manufacturers.

Competition. The mattress industry is highly competitive. Our business could be harmed by existing competitive pressures or from one or more new entrants into the market.

Our Sleep Number beds compete with a number of different types of mattress alternatives, including standard innerspring mattresses, foam mattresses, waterbeds, futons and other air-supported mattress products sold through a variety of channels, including home furnishings stores, specialty mattress stores, department stores, mass merchants, wholesale clubs, telemarketing programs, television infomercials and catalogs. The mattress industry is characterized by a high degree of concentration among the three largest manufacturers of innerspring mattresses with nationally recognized brand names, including Sealy, which also owns the Stearns & Foster brand, Serta and Simmons. Numerous other manufacturers, primarily operating on a regional or niche basis, serve the balance of the mattress market. Tempur-Pedic International, Inc. and other companies compete in the mattress industry with foam mattress products. A number of mattress manufacturers, including Sealy and Simmons, as well as a number of smaller manufacturers, including low-cost foreign manufacturers, have offered air beds that compete with our products.

We believe that many of our competitors, including in particular the three largest innerspring mattress manufacturers and Tempur-Pedic, have greater financial, marketing and manufacturing resources and better brand name recognition than we do and sell products through broader and more established distribution channels. Our stores and other company-controlled distribution channels compete with other retailers who often provide a wider selection of mattress alternatives than we offer through our channels of distribution, which may place our channels of distribution at a competitive disadvantage. These manufacturing and retailing competitors, or new entrants into the market, may compete aggressively and gain market share with existing and new mattress products, and may pursue or expand their presence in the air bed segment of the market. Some competitors may engage in aggressive advertising strategies that may include false or misleading claims about competitive products and/or our products. Any such competition could inhibit our ability to retain or increase market share, inhibit our ability to maintain or increase prices and reduce our margins, which could harm our sales, profitability and financial condition.

<u>Need for Continuous Product Improvement</u>. If we are unable to enhance our existing products and develop and market new products that respond to customer needs and achieve market acceptance, we may not be able to regain growth in sales or improvement in profitability.

One of our growth strategies is to continue to lead our industry in product innovation and sleep expertise by enhancing existing products and by developing and marketing new products that deliver personalized comfort and better sleep. We may not be successful in developing or marketing enhanced or new products that will receive acceptance in the marketplace. Further, the resulting level of sales from any of our enhanced or new products may not justify the costs associated with the development and marketing. Any failure to continue to develop and market enhanced or new products in a cost-effective manner could harm our ability to regain growth in sales or growth in profitability.

<u>Adequacy of Management Information Systems</u>. In December 2008, we abandoned plans to implement an SAP®-based enterprise-wide information technology architecture. As a result, we are currently enhancing our existing management information systems to support our existing and anticipated business needs and to comply with evolving payment card industry and state and federal regulatory standards applicable to data privacy and security. This project may take longer and may require more resources to implement than anticipated, may cause distraction of key personnel, and may cause disruptions to our business. Any of these outcomes could impair our ability to achieve critical strategic initiatives and could harm our sales, profitability and financial condition.

We depend upon our management information systems for many aspects of our business. Our current information systems architecture includes some off-the-shelf programs as well as some key software that has been developed by our own programmers, which is not easily modified or integrated with other software and systems and limits the flexibility and scalability of our information systems. Our business will be adversely affected if our management information systems are disrupted or if we are unable to improve, upgrade, integrate or expand our systems to meet business and regulatory requirements. In addition, any failure of our systems and processes to adequately protect customer information from theft or loss could adversely impact our business, reputation, sales, profitability and financial condition.

<u>Risks of Compliance with Governmental Regulations</u>. We are subject to a wide variety of government regulations. Any failure to comply with any of these regulations could harm our business, reputation, sales, profitability and financial condition. We may be required to incur significant expenses or to modify our operations in order to ensure compliance with these regulations.

We are subject to a wide variety of government regulations relating to the bedding industry or to various aspects of our business and operations, including without limitation:

- Regulations relating to the proper labeling of bedding merchandise and other aspects of product handling and sale;
- State regulations related to the proper labeling and sale of bedding products produced in part from refurbished components;
- Federal and state flammability standards applicable generally to mattresses and mattress and foundation sets;
- Federal safety standards applicable to children’s products generally, including some mattresses products;
- Environmental and product safety regulations;
- Consumer protection and data privacy regulations;
- Regulations related to marketing and advertising claims;
- Various federal and state “do not call” or “do not mail” list requirements;
- Federal, state and foreign labor laws, including but not limited to laws relating to occupational health and safety, employee privacy, wages and hours, overtime pay, harassment and discrimination, equal opportunity, and employee leaves and benefits;
- Antitrust regulations in the United States and foreign jurisdictions where we distribute our products;
- Import and export regulations;

- Federal and state tax laws; and
- Federal and state securities laws.

Although we believe that we are in compliance in all material respects with these regulations and have implemented a variety of measures to promote continuing compliance, regulations may change over time and we may be required to incur expenses and/or to modify our operations in order to ensure compliance with these regulations, which could harm our profitability and financial condition. If we are found to be in violation of any of the foregoing laws or regulations, we could become subject to fines, penalties, damages or other sanctions, as well as potential adverse public relations, which could adversely impact our business, reputation, sales, profitability and financial condition.

Risks of Compliance with Flammability Standards. All mattresses and mattress and foundation sets, including ours, became subject to new federal flammability standards and related regulations in July 2007. Compliance with these regulations has increased our product costs, has required modifications to our systems and operations and may increase the risk of disruptions to our business due to ongoing testing to assure compliance or due to regulatory inspections.

The federal Consumer Product Safety Commission adopted new flammability standards and related regulations which became effective nationwide in July 2007 for mattresses and mattress and foundation sets. Compliance with these requirements has resulted in higher materials and manufacturing costs for our products, and has required modifications to our information systems and business operations, further increasing our costs. To the extent we are unable to offset increased costs through value engineering and similar initiatives, or through price increases, our profitability may be adversely impacted. If we choose to increase prices to offset the increased costs, our unit sales volumes could be adversely impacted.

Compliance also requires more complicated manufacturing processes, which may reduce our manufacturing capacity and may require us to expand our manufacturing capacity sooner than otherwise anticipated.

The new regulations require manufacturers to implement quality assurance programs and encourage manufacturers to conduct random testing of products. The new regulations also require maintenance and retention of compliance documentation. These quality assurance and documentation requirements are costly to implement and maintain. If any product testing yields results indicating that any of our products may not meet the flammability standard, or if we obtain test results or other evidence that any of our products may fail to meet the standard or that a material or process used in manufacturing could affect the test performance of our product, we may be required to temporarily cease production and distribution and/or to recall products from the field, and we may be subject to fines or penalties, any of which outcomes could harm our business, reputation, sales, profitability and financial condition. We may also face increased risks of disruptions to our business caused by regulatory inspections.

Risks of Compliance with Safety Standards. All children's products, including some mattresses, are subject to new consumer product safety standards. Compliance with these regulations may increase our product costs and may require modifications to our systems and operations.

The Consumer Product Safety Improvement Act (CPSIA) establishes new lead and phthalates content standards for certain children's products, including some mattresses. Portions of the CPSIA, including compliance with the component content standards are effective February 10, 2009. The Consumer Product Safety Commission has stayed the enforcement of the testing and certification requirements for the component testing and certification until February 10, 2010. Compliance with these regulations may increase our product costs and may require modifications to our systems and operations.

Risks of Seasonal Influences. Our business is subject to seasonal influences and a substantial portion of our net sales is often realized in the last month or last few weeks of a quarter, due in part to our promotional schedule and commission structure. As our marketing expenditures are largely based on our expectations of future customer inquiries and net sales, and cannot be adjusted quickly, a failure to meet these expectations may harm our profitability and financial condition.

Our business is subject to some seasonal influences, with typically lower sales in the second quarter, and increased sales during selected holiday or promotional periods. Furthermore, a substantial portion of our sales is often realized in the last month or last few weeks of a quarter, due in part to our promotional schedule and commission structure. The level of our marketing and advertising expenses is based, in significant part, on our expectations of future customer inquiries and net sales

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and cannot be adjusted quickly. If there is a shortfall in expected net sales or in the conversion rate of customer inquiries, we may be unable to adjust our spending in a timely manner and our sales, profitability and financial condition may be harmed.

Product Returns and Warranty Claims. Significant and unexpected return rates under our 30-night trial period, or significant and unexpected warranty claims under our 20-year limited warranty, could harm our sales, profitability and financial condition.

Part of our marketing and advertising strategy focuses on providing a 30-night trial in which customers may return their beds and obtain a refund of the purchase price if they are not fully satisfied with our product. Return rates may not remain within acceptable levels. An unexpected increase in return rates could harm our sales, profitability and financial condition. We also provide our customers with a 20-year limited warranty on our beds. We may receive significant and unexpected claims under these warranty obligations that could exceed our warranty reserves. Warranty claims in excess of our warranty reserves could harm our profitability and financial condition.

Exposure to Product Liability Claims. We may face exposure to product liability claims.

We face an inherent business risk of exposure to product liability claims in the event that the use of any of our products is alleged to have resulted in personal injury or property damage. In the event that any of our products proves to be defective, we may be required to recall or redesign such products. In 2004 and in 2008, we experienced increased returns and adverse impacts on sales, as well as product liability litigation, as a result of media reports related to the alleged propensity of our products to develop mold. We may experience material increases in returns and material adverse impacts on sales or additional litigation in the event any similar media reports were to occur in the future. We maintain insurance against product liability claims, but such coverage may not continue to be available on terms acceptable to us and may not be adequate for liabilities actually incurred. A successful claim brought against us in excess of available insurance coverage, or any claim or product recall that results in significant adverse publicity against us, may have a material adverse effect on our business.

Protection of Our Intellectual Property. If we are unable to protect our intellectual property, we may be unable to prevent other companies from using our technology in competitive products.

We own various U.S. and foreign patents and patent applications related to certain elements of the design and function of our beds and related products. We also own several registered and unregistered trademarks and trademark applications, including in particular our Select Comfort and Sleep Number trademarks, which we believe have significant value and are important to the marketing of our products to customers. In addition to patents and trademarks, we rely upon copyrights, trade secrets and other intellectual property rights and we have implemented several measures to protect our intellectual property and confidential information contained in our products, such as entering into assignment of invention and nondisclosure agreements with certain of our employees. Our ability to compete effectively with other companies depends, to a significant extent, upon our ability to maintain the proprietary nature of our owned intellectual property and confidential information. Our intellectual property rights may not provide substantial protection against infringement or piracy and may be circumvented by our competitors. Our protective measures may not protect our intellectual property rights or confidential information or prevent our competitors from developing and marketing products that are similar to or competitive with our beds or other products. In addition, the laws of some foreign countries may not protect our intellectual property rights and confidential information to the same extent as the laws of the United States. If we are unable to protect our intellectual property, we may be unable to prevent other companies from using our technology or trademarks in connection with competitive products, which could adversely affect our sales, profitability and financial condition.

Intellectual property litigation, which could result in substantial costs to us and the diversion of significant time and effort by our executive management, may be necessary to enforce our patents and trademarks and to protect our trade secrets and proprietary technology. We may not have the financial resources necessary to enforce or defend our intellectual property rights.

We are not aware of any material intellectual property infringement or invalidity claims that may be asserted against us, however, it is possible that third parties, including competitors, may successfully assert such claims. The cost of defending such claims, or any resulting liability, or any failure to obtain necessary licenses on reasonable terms, may adversely impact our sales, profitability and financial condition.

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Dependence on Management and Other Key Employees. The loss of the services of any members of our executive management team could adversely impact our ability to execute our business strategy and growth initiatives and could harm our business.

We are currently dependent upon the continued services, ability and experience of our executive management team, particularly William R. McLaughlin, our Chief Executive Officer. The loss of the services of Mr. McLaughlin or any other member of our executive management team could have an adverse effect on our ability to execute our business strategy and growth initiatives and on our sales, profitability and financial condition. We do not maintain any key person life insurance on any members of our executive management team. Our future growth and success will also depend upon our ability to attract, retain and motivate other qualified personnel.

NASDAQ Listing Requirements. Failure to satisfy NASDAQ Global Select Market listing requirements may result in our common stock being removed from listing on the NASDAQ Global Select Market.

Our common stock is currently listed on the NASDAQ Global Select Market under the symbol “SCSS.” For continued inclusion on the NASDAQ Global Select Market, we must generally maintain, among other requirements, either (a) shareholders’ equity of at least $10 million, a minimum closing bid price of $1.00 per share and a market value of our public float of at least $5 million; or (b) market capitalization of at least $50 million, a minimum closing bid price of $1.00 per share and a market value of our public float of at least $15 million. We currently do not meet these minimum closing bid price and market capitalization requirements. NASDAQ has recently suspended enforcement, through April 20, 2009, of the rules requiring a minimum closing bid price and a minimum market value of public float. After April 20, 2009, however, if we fail to meet the minimum closing bid price or the minimum market value standards described above for at least 30 consecutive trading days, our common stock could be at risk of being removed from listing on the NASDAQ Global Select Market. If our common stock were removed from listing on the NASDAQ Global Select Market, our common stock may be transferred to the NASDAQ Capital Market if we satisfy the listing criteria for the NASDAQ Capital Market, or trading of our common stock may be conducted in the over-the-counter market in the so-called “pink sheets” or, if available, the National Association of Securities Dealer’s “Electronic Bulletin Board.” Consequently, broker-dealers may be less willing or able to sell and/or make a market in our common stock, which may make it more difficult for shareholders to dispose of, or to obtain accurate quotations for the price of, our common stock. Removal of our common stock from listing on the NASDAQ Global Select Market may also make it more difficult for us to raise capital through the sale of our securities.

Risks of International Distribution. Through relationships with other parties, we distribute products in Canada and Australia, which presents some additional risks to our business.

To date, the vast majority of our sales have been made in the U.S. and we have sold only very minimal quantities of products in foreign jurisdictions. In late 2005 we began to distribute our products in Canada through an independent retailer. In late 2007 we entered into relationships with an Australian-based manufacturer and an Australian-based retailer to begin distribution of Sleep Number beds in Australia and New Zealand. Our lack of experience in international distribution presents some risks to our business, including without limitation the need to build awareness of our products and brand in new markets, the need to gain market acceptance for new products that represent a significant departure from traditional bedding products, logistical and systems complexities, different levels of protection of our intellectual property, language and cultural differences, the need to comply with additional and different regulatory requirements, foreign currency exchange risks and political instability.

Although several members of our senior management team have significant experience in international distribution of consumer goods, as a company our experience in this area is limited. The current economic environment and its impact on our business has limited our ability to invest in our international infrastructure, which may adversely impact the sales and profitability of our international operations, as well as the timing of additional international expansion. If we are unable to achieve consumer awareness and market acceptance for our products in foreign jurisdictions, we may not be able to achieve sufficient sales and profitability in our international operations to justify the investment.

Risks of Terrorist Attacks. Additional terrorist attacks in the United States or against U.S. targets, or acts of war or threats of war or the escalation of current hostilities involving the United States or its allies could adversely impact our sales, profitability, financial condition or stock price in unpredictable ways.

Additional terrorist attacks in the United States or against U.S. targets, or acts of war or threats of war or the escalation of current hostilities involving the United States or its allies, or military or trade disruptions impacting our domestic or foreign suppliers of components of our products, may adversely impact our operations, including, but not limited to, causing delays or losses in the delivery of merchandise to us and decreased sales of our products. These events could cause an increase in oil or other commodity prices, which could adversely affect our materials or transportation costs, including the costs of delivery of our products to customers. More generally, any of these events could adversely impact consumer confidence and spending or result in increased volatility in the U.S. and worldwide financial markets. These events also could cause, or deepen and prolong, an economic recession in the United States or abroad. Any of these occurrences could have an adverse impact on our sales, profitability and financial condition, and may result in volatility of our stock price.

Risks of Pandemic. An outbreak of Avian Flu or a pandemic, or the threat of a pandemic, may adversely impact our ability to produce and deliver our products or may adversely impact consumer demand.

Concern has grown recently over the possibility of a significant or global outbreak of avian flu or a similar pandemic. A significant outbreak of avian flu, or a similar pandemic, or even a perceived threat of such an outbreak, could cause significant disruptions to our supply chain, manufacturing capability and distribution system that could adversely impact our ability to produce and deliver products, which could result in a loss of sales and adversely impact on our profitability and financial condition. Similarly, such events could adversely impact consumer confidence and consumer demand generally, which could adversely impact our sales, profitability and financial condition.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Distribution Locations

We currently lease all of our existing retail store locations and expect that our policy of leasing, rather than owning stores will continue. Our store leases generally provide for an initial lease term of five to seven years with a mutual termination option if we do not achieve certain minimum annual sales thresholds. Generally, the store leases require us to pay minimum rent plus percentage rent based on net sales in excess of certain thresholds, as well as certain operating expenses.

The following table summarizes the geographic location of our 471 company-owned stores and 801 retail partner doors as of January 3, 2009:

	Company-Owned Stores	Retail Partner Doors		Company Owned Stores	Retail Partner Doors
Alabama	5	-	Montana	3	-
Alaska	-	3	Nebraska	3	-
Arizona	12	41	Nevada	4	25
Arkansas	4	-	New Hampshire	5	-
California	48	148	New Jersey	14	-
Colorado	16	-	New Mexico	2	-
Connecticut	6	-	New York	15	-
Delaware	2	-	North Carolina	13	31
Florida	33	56	North Dakota	2	-
Georgia	17	38	Ohio	20	17
Hawaii	-	6	Oklahoma	3	6
Idaho	1	-	Oregon	4	25
Illinois	22	-	Pennsylvania	19	-
Indiana	13	13	Rhode Island	1	-
Iowa	6	-	South Carolina	6	7
Kansas	5	4	South Dakota	2	-
Kentucky	4	2	Tennessee	9	14
Louisiana	5	5	Texas	39	166
Maine	2	-	Utah	4	-
Maryland	12	-	Vermont	1	-
Massachusetts	8	-	Virginia	13	-
Michigan	14	-	Washington	13	49
Minnesota	15	-	West Virginia	1	-
Mississippi	2	2	Wisconsin	10	-
Missouri	13	9	Wyoming	-	-
			Canada	-	134
			Total	471	801

Manufacturing and Headquarters

We lease our 159,000-square-foot corporate headquarters in Minneapolis, Minnesota. The lease commenced in November 2007 and runs through 2017 with two five-year renewal options.

We also lease approximately 122,000 square feet in Minneapolis, Minnesota that includes our direct marketing call center, our customer service group, our research and development department, and a distribution center that accepts returns and processes warranty claims. This lease expires in 2017 and contains one five-year renewal option.

We lease two manufacturing and distribution centers in Irmo, South Carolina and Salt Lake City, Utah of approximately 105,000 square feet and approximately 101,000 square feet, respectively. We lease the Irmo facility through February 2013, and the Salt Lake City facility through April 2010, with a five-year renewal option thereafter.

To support our accessories business and our program with Radisson Hotels and Resorts, we lease approximately 40,000 square feet in Omaha, Nebraska, through July 2009. We plan to close this facility in 2009 and relocate its operations to our Minneapolis distribution center.

ITEM 3. LEGAL PROCEEDINGS

On April 25, 2008, a lawsuit was filed against one of our subsidiaries in Superior Court in Santa Clara County, California by one of our customers. The complaint asserted various claims related to products liability, breach of warranty, concealment, intentional misrepresentation and negligent misrepresentation and sought class certification. The complaint alleged that products sold by us prior to 2006 had a unique propensity to develop mold, alleged that the plaintiff suffered adverse health effects, and sought various forms of legal and equitable relief, including without limitation unspecified damages, punitive and exemplary damages, attorneys' fees and costs, and injunctive relief. We removed the case to the U.S. District Court for the Northern District of California. On September 30, 2008, the Court granted our motion to dismiss and strike the purported class action claims, and allowed the plaintiff leave to amend the complaint. On October 30, 2008, the plaintiff filed an amended complaint alleging facts similar to those asserted in the initial complaint and asserting additional claims, including antitrust and RICO claims. We have filed a motion to dismiss the amended complaint on the same basis that the Court dismissed the original complaint, and our motion remains pending before the Court. As of January 3, 2009, no accrual had been established as we believe that the complaint is without merit and we intend to vigorously defend the claims.

We are involved from time to time in various other legal proceedings arising in the ordinary course of our business, including primarily commercial, employment and intellectual property claims. In accordance with generally accepted accounting principles in the United States, we record a liability in our consolidated financial statements with respect to any of these matters when it is both probable that a liability has been incurred and the amount of the liability can be reasonably estimated. With respect to these other matters, we believe that we have valid defenses to claims asserted against us and we do not expect the outcome of these other matters to have a material effect on our results of operations or financial position. Litigation, however, is inherently unpredictable, and it is possible that the ultimate outcome of one or more claims asserted against us could adversely impact our results of operations or financial position.

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

Not applicable.

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock trades on The NASDAQ Stock Market LLC (NASDAQ Global Select Market) under the symbol "SCSS." As of February 28, 2009, there were approximately 799 holders of record of our common stock. The following table sets forth the quarterly high and low sales prices per share of our common stock as reported by NASDAQ for the two most recent fiscal years. These quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission, and may not necessarily represent actual transactions.

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Fiscal 2008				
High	$ 1.96	$ 2.83	$ 3.97	$ 8.32
Low	0.19	1.16	1.47	3.10
Fiscal 2007				
High	$ 14.75	$ 18.00	$ 19.03	$ 20.17
Low	6.11	13.90	15.94	16.77

Select Comfort has not historically paid cash dividends on its common stock and is restricted from paying dividends under its credit agreement.

Information concerning stock repurchases completed during the fourth quarter of fiscal 2008 is set forth below:

Fiscal Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
September 28, 2008 through October 25, 2008	—	—	—	
October 26, 2008 through November 29, 2008	—	—	—	
November 30, 2008 through	—	—	—	$ 206,762,000

January 3, 2009			
Total	—	—	—

(1) On April 20, 2007, our Board of Directors authorized the company to repurchase up to an additional $250.0 million of its common stock, bringing the total availability under our share repurchase program to $290.0 million. The Finance Committee of the Board of Directors reviews repurchases under this program on a quarterly basis. There is no expiration date governing the period over which we can repurchase shares. As of January 31, 2009, the total outstanding authorization was $206.8 million. We may terminate or limit the stock repurchase program at any time. We currently have no plans to repurchase shares under this authorization.

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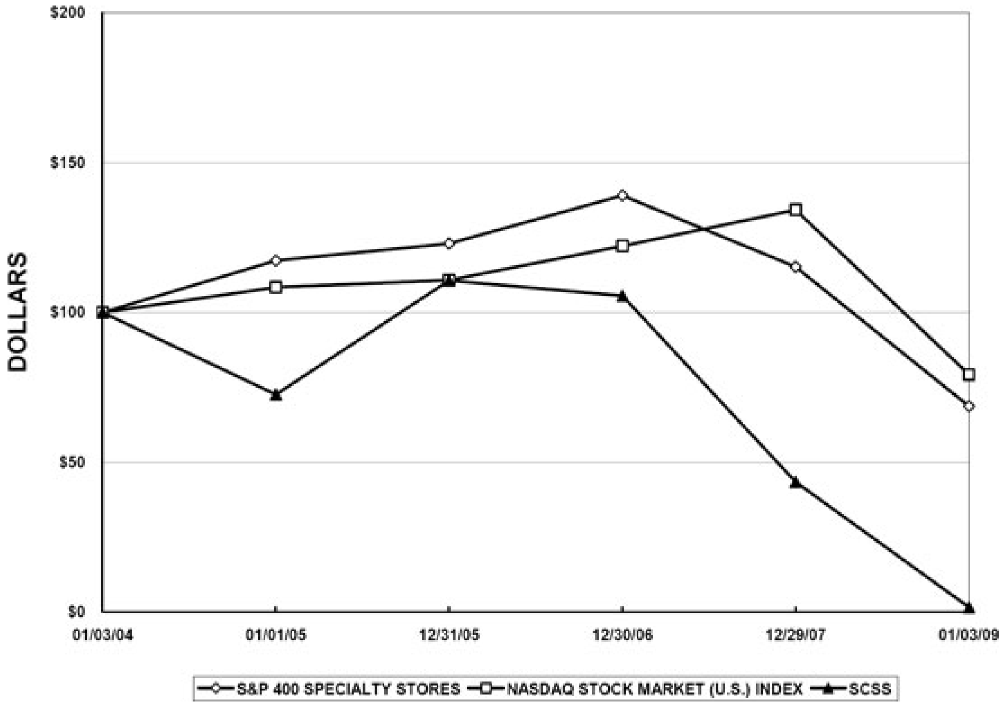
Comparative Stock Performance

The graph below compares the total cumulative shareholder return on our common stock over the last five years to the total cumulative return on the Standard and Poor's ("S&P") 400 Specialty Stores Index and The NASDAQ Stock Market (U.S.) Index assuming a $100 investment made on January 3, 2004. Each of the three measures of cumulative total return assumes reinvestment of dividends. The stock performance shown on the graph below is not necessarily indicative of future price performance. The information contained in this "Comparative Stock Performance" section shall not be deemed to be "soliciting material" or "filed" or incorporated by reference in future filings with the SEC, or subject to the liabilities of Section 18 of the Securities Exchange Act of 1934, as amended, except to the extent that we specifically request that it be treated as soliciting material or incorporate it by reference into a document filed under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.

COMPARISON OF FIVE-YEAR CUMULATIVE TOTAL RETURN AMONG SELECT COMFORT CORPORATION, S&P 400 SPECIALTY STORES INDEX, AND THE NASDAQ STOCK MARKET (U.S.) INDEX



	1/3/2004	1/1/2005	12/31/2005	12/30/2006	12/29/2007	1/3/2009
Select Comfort Corporation	$ 100	$ 73	$ 111	$ 106	$ 43	$ 2
S&P 400 Specialty Stores Index	100	117	123	139	115	69
The NASDAQ Stock Market (U.S.) Index	100	108	111	122	134	79

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Securities Authorized for Issuance under Equity Compensation Plans

The following table summarizes information about our equity compensation plans as of January 3, 2009:

EQUITY COMPENSATION PLAN INFORMATION

Plan Category	Number of securities to be issued upon exercise of	Weighted average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity

	outstanding options, warrants and rights[1]		compensation plans (excluding securities reflected in the first column)
Equity compensation plans approved by security holders	5,074,000	$10.67	1,435,000
Equity compensation plans not approved by security holders	None	Not applicable	None
Total	5,074,000	$10.67	1,435,000

(1) Includes the Select Comfort Corporation 1990 Omnibus Stock Option Plan, the Select Comfort Corporation 1997 Stock Incentive Plan and the Select Comfort Corporation 2004 Stock Incentive Plan.

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ITEM 6. SELECTED FINANCIAL DATA
(in thousands, except per share and selected operating data, unless otherwise indicated)

The Consolidated Statements of Operations Data and Consolidated Balance Sheet Data presented below have been derived from our Consolidated Financial Statements and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our Consolidated Financial Statements and Notes thereto included in this Annual Report on Form 10-K.

	Year					
	2008[2]	**2007**	**2006[1]**	**2005**	**2004**	**2003[2]**
Consolidated Statements of Operations Data:						
Net sales	$ 608,524	$ 799,242	$ 806,038	$ 689,548	$ 557,639	$ 458,489
Gross profit	358,572	486,415	490,508	406,476	339,838	285,324
Operating expenses:						
Sales and marketing	332,068	372,467	341,630	286,206	250,628	207,400
General and administrative	57,994	64,351	65,401	49,300	37,826	33,974
Research and development	3,374	5,682	4,687	2,219	1,853	1,295
Asset impairment charges	34,594	409	5,980	162	—	71
Operating (loss) income	(69,458)	43,506	72,810	68,589	49,531	42,584
Net (loss) income	$ (70,177)	$ 27,620	$ 47,183	$ 43,767	$ 31,555	$ 27,102
Net (loss) income per share:						
Basic	$ (1.59)	$ 0.59	$ 0.89	$ 0.82	$ 0.58	$ 0.55
Diluted	(1.59)	0.57	0.85	0.76	0.53	0.46
Shares used in calculation of net income per share:						
Basic	44,186	46,536	52,837	53,357	54,015	49,157
Diluted	44,186	48,292	55,587	57,674	59,525	58,916
Consolidated Balance Sheet Data:						
Cash, cash equivalents and marketable debt securities	$ 13,057	$ 7,279	$ 90,175	$ 123,091	$ 101,963	$ 75,118
Working capital	(90,534)	(70,000)	5,637	10,158	23,479	53,972
Total assets	135,413	190,489	228,961	239,838	202,033	153,506
Borrowings under revolving credit facility	79,150	37,890	—	—	—	—
Capital lease obligations (non-current)	621	—	—	—	—	—
Total shareholders' (deficit) equity	(41,630)	24,126	115,694	121,347	114,344	92,201
Selected Operating Data:						
Stores open at period-end[3]	471	478	442	396	370	344
Stores opened during period	19	45	51	40	31	27
Stores closed during period	26	9	5	14	5	5
Retail partner doors	801	891	822	353	89	77
Average net sales per store (000's)[4]	$ 984	$ 1,318	$ 1,493	$ 1,417	$ 1,247	$ 1,101
Percentage of stores with more than $1.0 million in net sales[4]	45%	73%	81%	77%	64%	49%
Comparable-store sales (decrease) increase[5]	(25%)	(11%)	7%	15%	16%	31%
Average square footage per store open during period[4]	1,410	1,315	1,200	1,121	1,032	990
Net sales per square foot[4]	$ 703	$ 1,024	$ 1,244	$ 1,264	$ 1,208	$ 1,113
Average store age (in months at period end)	91	84	81	79	75	70

(1) In the first quarter of fiscal 2006, we adopted the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 123R, "*Share-Based Payment*," requiring us to recognize expense related to the fair value of our stock-based compensation awards. We elected the modified prospective transition method and, accordingly, financial results for fiscal years prior to 2006 have not been restated. Stock-based compensation expense for fiscal 2008, 2007 and 2006 was $3,702, $6,252 and $8,325, respectively. Prior to the adoption of SFAS No. 123R, we followed the intrinsic value

method in accordance with Accounting Principles Board ("APB") Opinion No. 25, "*Accounting for Stock Issued to Employees,*" to account for our employee stock options and employee stock purchase plan. Accordingly, no compensation expense was recognized for share purchase rights granted in connection with the issuance of stock options under our employee stock option plan or employee stock purchase plan; however, compensation expense was recognized in connection with the issuance of restricted and performance shares granted. See Note 6 of the Notes to the Consolidated Financial Statements for additional information regarding stock-based compensation. Stock-based compensation expense (pre-tax) recognized in our financial results for years prior to fiscal 2006 was $793, $405, and $76 in 2005, 2004 and 2003, respectively.

(2) Fiscal years 2008 and 2003 had 53 weeks. All other fiscal years presented had 52 weeks.

(3) Includes stores operated in leased departments within other retail stores (none in 2008, 2007, 2006 and 2005; and 13 in 2004 and 2003).

(4) For stores open during the entire period indicated.

(5) Stores are included in the comparable-store calculation in the 13th full month of operation. Stores that have been remodeled or relocated within the same shopping center remain in the comparable-store base. The number of comparable-stores used to calculate such data was 452, 432, 391, 354, 339, and 316 for 2008, 2007, 2006, 2005, 2004 and 2003, respectively. Our 2008 comparable-store sales decrease reflects adjustments for an additional week of sales. Without adjusting for the additional week, comparable-stores sales would have decreased (25%) for 2008. Our 2004 and 2003 comparable-store sales increase reflects adjustments for an additional week of sales in 2003. Without adjusting for the additional week, comparable-store sales would have been 14% for 2004 and 34% for 2003.

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

The discussion in this Annual Report contains certain forward-looking statements that relate to future plans, events, financial results or performance. You can identify forward-looking statements by those that are not historical in nature, particularly those that use terminology such as "may," "will," "should," "could," "expect," "anticipate," "believe," "estimate," "plan," "project," "predict," "intend," "potential," "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 our historical experience and our present expectations or projections. These risks and uncertainties include, among others:

- ***Our current lack of adequate liquidity and capital resources and our ability to continue as a going concern;***
- ***Current general and industry economic trends;***
- ***Consumer confidence;***
- ***The effectiveness of our marketing messages;***
- ***The efficiency of our advertising and promotional efforts;***
- ***Consumer acceptance of our products, product quality, innovation and brand image;***
- ***Availability of attractive and cost-effective consumer credit options;***
- ***Execution of our retail distribution strategy, including our ability to cost-effectively close under-performing store locations;***
- ***Our dependence on significant suppliers and our ability to maintain relationships with key suppliers, including several sole source suppliers;***
- ***The vulnerability of key suppliers to recessionary pressures, labor negotiations, liquidity concerns or other factors;***
- ***Rising commodity costs and other inflationary pressures;***
- ***Industry competition;***
- ***Our ability to continue to improve our product line;***
- ***Warranty expenses;***
- ***Pending and potentially unforeseen litigation;***
- ***Increasing government regulations, including new flammability standards for the bedding industry and new safety standards for consumer products;***
- ***The adequacy of our management information systems to meet the evolving needs of our business and evolving regulatory standards applicable to data privacy and security;***
- ***Our ability to attract and retain senior leadership and other key employees, including qualified sales professionals; and***
- ***Global events, such as terrorist attacks or a pandemic outbreak, or the threat of such events.***

Additional information concerning these and other risks and uncertainties is contained under the caption "Risk Factors" in this Annual Report on Form 10-K.

Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to provide a reader of our financial statements with a narrative from the perspective of management on our financial condition, results of operations, liquidity and certain other factors that may affect our future results. Our MD&A is presented in seven sections:

- Overview
- Results of Operations

- Liquidity and Capital Resources
- Outlook
- Off-Balance-Sheet Arrangements and Contractual Obligations
- Critical Accounting Policies and Estimates
- Recent Accounting Pronouncements

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Overview

Business Overview

Select Comfort 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 for consumers.

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 and through leading home furnishings retailers, specialty bedding retailers, the QVC shopping channel and to several end users such as Radisson Hotels and Resorts®.

Vision and Strategy

Our vision is to be a leading brand in the bedding industry, while improving people's lives through better sleep.

We are executing against a defined strategy which focuses on the following key components:
- Building brand awareness and increasing store traffic through effective marketing programs;
- Managing our business in the current economic environment through disciplined controls over costs and cash;
- Accelerating product innovation to lead the industry in innovative sleep products; and
- Leveraging our infrastructure in order to facilitate long-term profitability.

Results of Operations

Fiscal 2008 Summary

Financial highlights for the fiscal year ended January 3, 2009 were as follows:

- Net loss totaled $70.2 million, or $(1.59) per diluted share, compared with net income of $27.6 million, or $0.57 per diluted share in 2007. The 2008 net loss includes non-cash charges for asset impairments totaling $34.6 million and establishment of a $26.8 million valuation allowance for deferred taxes.

- Net sales decreased 24% to $608.5 million, compared with $799.2 million for the prior year, primarily due to a 25% comparable-store sales decline in our company-owned retail stores.

- Our 2008 gross profit rate decreased to 58.9% compared with 60.9% for the prior year. The gross profit rate decrease was primarily due to higher commodity and logistics costs including the impact of higher fuel prices, increased material costs for compliance with new fire retardancy standards and for our new bed line launched last year, and the deleveraging impact of the 24% net sales decrease.

- Sales and marketing expenses decreased by $40.4 million, but increased to 54.6% of net sales in 2008, compared with 46.6% of net sales for the prior fiscal year. The rate increase was driven by the deleveraging impact of the 24% net sales decrease.

- General and administrative expenses declined $6.4 million compared with the prior year primarily due to workforce reductions and other cost reduction initiatives.

- Cash provided by operating activities in 2008 totaled $3.0 million, compared with $44.0 million for the prior year.

- During 2008, borrowings under our revolving credit facility increased from $37.9 million at December 29, 2007 to $79.2 million at January 3, 2009. We have taken significant actions designed to stabilize sales, reduce our cost structure and improve profitability. We also have been exploring a range of strategic and financing alternatives to enhance our financial flexibility and maintain our liquidity. If we are unable to obtain additional capital, we may not be able to fund our operating needs and we could face a risk of default under our credit agreement.

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The following table sets forth, for the periods indicated, our results of operations expressed as dollars and percentages of net sales. Figures are in millions except percentages and earnings per share amounts. Amounts may not add due to rounding differences.

	2008		2007		2006	
	$	% of Net Sales	$	% of Net Sales	$	% of Net Sales
Net sales	$ 608.5	100.0%	$ 799.2	100.0%	$ 806.0	100.0%
Cost of sales	250.0	41.1	312.8	39.1	315.5	39.1

Gross profit	358.6	58.9	486.4	60.9	490.5	60.9
Operating expenses:						
Sales and marketing	332.1	54.6	372.5	46.6	341.6	42.4
General and administrative	58.0	9.5	64.4	8.1	65.4	8.1
Research and development	3.4	0.6	5.7	0.7	4.7	0.6
Asset impairment charges	34.6	5.7	0.4	0.1	6.0	0.7
Total operating expenses	428.0	70.3	442.9	55.4	417.7	51.8
Operating (loss) income	(69.5)	(11.4)	43.5	5.4	72.8	9.0
Other (expense) income, net	(3.3)	(0.5)	—	—	3.0	0.4
(Loss) income before income taxes	(72.7)	(12.0)	43.5	5.4	75.8	9.4
Income tax (benefit) expense	(2.6)	(0.4)	15.8	2.0	28.6	3.6
Net (loss) income	$ (70.2)	(11.5%)	$ 27.6	3.5%	$ 47.2	5.9%

	2008	2007	2006
Net (loss) income per share:			
Basic	$ (1.59)	$ 0.59	$ 0.89
Diluted	(1.59)	0.57	0.85
Weighted-average number of common shares:			
Basic	44.2	46.5	52.8
Diluted	44.2	48.3	55.6

The proportion of our total net sales, by dollar volume, from each of our channels during the last three years was as follows:

	2008	2007	2006
Retail	78.2%	75.4%	76.2%
Direct	7.7%	8.0%	9.4%
E-Commerce	6.1%	6.8%	5.6%
Wholesale	8.0%	9.8%	8.8%
Total	100.0%	100.0%	100.0%

The components of total net sales change, including comparable-store net sales changes, were as follows:

	2008 Channel increase/ (decrease)	2007 Channel increase/ (decrease)	2006 Channel increase
Comparable stores(1)	(25%)	(11%)	7%
Net new stores	4%	9%	9%
Retail total	(21%)	(2%)	16%
Direct	(26%)	(16%)	1%
E-Commerce	(32%)	20%	31%
Wholesale	(38%)	11%	40%
Total net sales change	(24%)	(1%)	17%

(1) Stores are included in the comparable-store calculation in the 13th full month of operation. Stores that have been remodeled or relocated within the same shopping center remain in the comparable-store base. Fiscal 2008 included 53 weeks, as compared to 52 weeks in fiscal 2007. Comparable-store sales have been adjusted and reported as if both years had the same number of weeks.

The number of company-owned retail stores during the last three years, and independently owned and operated retail partner stores, was as follows:

	2008	2007	2006
Company-owned retail stores:			
Beginning of year	478	442	396
Opened	19	45	51
Closed	(26)	(9)	(5)
End of year	471	478	442
Retail partner stores	801	891	822

Comparison of 2008 and 2007

Net Sales

Net sales in 2008 decreased 24% to $608.5 million, compared with $799.2 million in 2007. The sales decrease was due to a 25% comparable-store sales decline in our company-owned retail stores and decreases in wholesale, E-Commerce and direct channel sales, partially offset by sales from new company-owned retail stores opened in the past 12 months net of stores closed. Total sales of mattress units decreased 30% compared to 2007, while the average selling price per bed (mattress sales only divided by mattress units) in our company-controlled channels increased 4% to $1,764, while sales of other product and services decreased by 17%.

The $190.7 million net sales decrease compared with 2007 was comprised of the following: (i) a $127.1 million net decrease in sales from our company-owned retail stores, comprised of a $149.2 million decrease from comparable-stores and a $22.1 million increase from new stores, net of stores closed; (ii) a $29.5 million decrease in wholesale sales; (iii) a $17.6 million decrease in E-Commerce sales and (iv) a $16.5 million decrease in direct marketing sales.

Gross Profit

The gross profit rate decreased to 58.9% in 2008 compared with 60.9% in 2007. The majority of the gross profit rate decline was driven by higher commodity and logistics costs including the impact of higher fuel prices, increased production costs for our new line of beds and fire-retardant products launched last year, and the deleveraging impact of the 24% net sales decrease. In addition, a sales mix shift to lower margin products reduced the gross profit rate by approximately 0.4 percentage points ("ppt"), compared to the same period one year ago. These items were partially offset by an increase in the percentage of net sales from our retail distribution channel which increased the gross profit rate by approximately 0.5 ppt. Pricing initiatives implemented in our company-owned sales channels also favorably impacted our gross profit rate as compared to the prior year.

Sales and Marketing Expenses

Sales and marketing expenses in 2008 decreased to $332.1 million, or 54.6% of net sales, compared with $372.5 million, or 46.6% of net sales in 2007. The $40.4 million decrease was primarily due to the following: (i) a $17.9 million or 16% reduction in media spending compared with the same period one-year ago and (ii) reduced variable selling expenses due to the net sales decline including lower financing costs, percentage rents and variable store compensation. The 8.0 ppt sales and marketing expense rate increase was principally due to the deleveraging impact of the 24% net sales decline, partially offset by the $40.4 million expense decrease compared with the same period one year ago.

General and Administrative Expenses

General and administrative ("G&A") expenses decreased $6.4 million to $58.0 million in 2008, compared with $64.4 million in 2007, but increased to 9.5% of net sales, compared with 8.1% in the prior year. The $6.4 million decrease in G&A expenses was primarily due to workforce reductions, reduced stock-based compensation expense, lower depreciation expense and other discretionary spending reductions. The year-over-year decline in stock-based compensation expense was primarily due to an increase in our estimated forfeiture rates resulting from the workforce reductions.

Research and Development

Research and development ("R&D") expenses decreased to $3.4 million in 2008 compared with $5.7 million in 2007, and decreased as a percentage of net sales to 0.6% from 0.7%. Fiscal 2007 included additional R&D expenses related to the development of new fire retardant products and an upgrade of our entire line of bed models.

Asset Impairment Charges

Asset impairment charges increased to $34.6 million in 2008, compared with $0.4 million in 2007. During the fourth quarter of fiscal 2008, we elected to abandon our plan to implement an integrated suite of SAP®-based applications and recognized asset impairment charges totaling $27.6 million. During 2008, on a quarterly basis, we reviewed all of our stores for impairment and determined that certain store assets at underperforming stores were impaired. We recognized impairment charges totaling $7.0 million for the difference between the fair value and the carrying amounts of the related long-lived assets. The increase in store asset impairment charges compared to the prior year was due primarily to the deterioration of consumer spending and the more difficult economic environment. We estimate fair values based on the cash-flows expected to be generated by the assets.

During 2007, we determined that certain store assets at underperforming stores were impaired and recognized impairment charges of $0.4 million for the difference between fair value and the carrying amounts of the related long-lived assets.

Other (Expense) Income, Net

Other expense increased to $3.3 million compared with $40,000 in 2007. The $3.2 million increase in other expense was driven by increased interest expense from borrowings under our revolving line of credit due to higher average debt balances and increased interest rates, and lower average cash and investment balances compared to the same period one year ago.

Income Tax (Benefit) Expense

Income tax benefit in 2008 was $2.6 million compared with income tax expense of $15.8 million in 2007. The effective tax rate was (3.5%) and 36.5% in 2008 and 2007, respectively. The change in the effective income tax rate is primarily due to the establishment of a $26.8 million valuation allowance against our deferred tax assets that we recorded in the fourth quarter of fiscal 2008. The remainder of the change in the effective tax rate resulted from the absence of a manufacturing deduction that we realized in 2007 and a higher state income tax rate in 2008, partially offset by a $0.6 million discrete tax benefit adjustment recognized in 2008 related to research and development tax credits for prior years based on the recognition guidance under FASB Interpretations No. 48, *Accounting for Uncertainty in Income Taxes*.

Comparison of 2007 and 2006

Net Sales

Net sales in 2007 decreased 1% to $799.2 million, compared with $806.0 million in 2006. The sales decrease was due to an 11% comparable-store sales decline in our company-owned retail stores and a decrease in direct channel sales, partially offset by sales from 36 net new company-owned retail stores opened in the past 12 months and sales growth in our E-Commerce and wholesale distribution channels. Total sales of mattress units decreased 1% compared to 2006, and the average selling price per bed (mattress sales only divided by mattress units) in our company-controlled channels was essentially flat at $1,694, while sales of other product and services increased by 2%.

The $6.8 million net sales decrease compared with 2006 was comprised of the following: (i) a $12.2 million decrease in direct marketing sales and (ii) an $11.6 million net decrease in sales from our company-owned retail stores, comprised of a $66.3 million decrease from comparable-stores and a $54.7 million increase from new stores, net of stores closed, partially offset by, (iii) a $9.0 million increase in E-Commerce sales and (iv) an $8.0 million increase in wholesale sales.

Gross Profit

The gross profit rate of 60.9% in 2007 was consistent with the prior year. The gross profit rate benefited from improvements in sourcing, manufacturing productivity and our ongoing implementation of a hub-and-spoke logistics network which reduced our cost of sales. The gross profit rate also benefited from a reduction in warranty costs per unit.

These items were offset by increased costs to comply with the new open flame fire retardancy standards which became effective for all products manufactured after July 1, 2007 and increased production costs associated with our new line of beds. In addition, the gross profit rate was negatively impacted by a sales mix shift to lower margin products which reduced the gross profit rate by approximately 0.4 ppt.

Sales and Marketing Expenses

Sales and marketing expenses in 2007 increased to $372.5 million, or 46.6% of net sales, compared with $341.6 million, or 42.4% of net sales in 2006. The $30.9 million expense increase was primarily due to operating costs associated with 36 net new stores opened in the past 12 months, an increased use of promotional financing offers and increased media spending. The 4.2 ppt. sales and marketing expense rate increase was primarily due to the deleveraging impact of an 11% comparable-store sales decline and the $30.9 million expense increase compared with the prior year. Total media spending increased 4% compared with 2006 and was 0.7 ppt. higher on a rate basis.

General and Administrative Expenses

General and administrative expenses decreased $1.0 million to $64.4 million in 2007, compared with $65.4 million in 2006, and remained consistent with the prior year on a rate basis. G&A expenses were favorably impacted by a $3.7 million reduction in incentive-based compensation costs compared to the prior year, partially offset by an increase in other expenses of $2.7 million, including increased information technology expenses and occupancy costs.

Research and Development

Research and development expenses increased to $5.7 million in 2007 compared with $4.7 million in 2006, and increased as a percentage of net sales to 0.7% from 0.6%. The dollar and percentage of net sales increases in R&D expenses were the result of continued investment in new product innovation and increased development costs to comply with the new open flame fire retardancy standards.

Asset Impairment Charges

Asset impairment charges decreased to $0.4 million in 2007, compared with $6.0 million in 2006. The 2007 asset impairment charges primarily related to assets at underperforming stores. The 2006 asset impairment charges included $5.4 million for abandoned software in connection with our decision to implement a new SAP® enterprise resource planning system, and $0.6 million related to assets at underperforming stores.

Other (Expense) Income, Net

Other expense was flat in 2007, compared with $3.0 million of other income in 2006. The $3.0 million decrease was driven by lower average cash and investment balances compared with 2006 which resulted in reduced interest income, increased interest expense from borrowings under our revolving line of credit to fund 2007 common stock repurchases and $0.3 million of net realized losses on the sales of marketable debt securities.

Income Tax Expense

Income tax expense decreased to $15.8 million in 2007, compared with $28.6 million in 2006. The effective tax rate was 36.5% and 37.8% in 2007 and 2006, respectively. The lower effective tax rate in 2007 was primarily due to research and development income tax credits recognized in 2007 based on federal tax law changes, and increased tax benefit related to manufacturing deductions.

Liquidity and Capital Resources

As of January 3, 2009, we had cash and cash equivalents of $13.1 million compared with $7.3 million as of December 29, 2007. The $5.8 million increase in cash and cash equivalents was primarily due to $3.0 million of cash provided by operating activities and a $35.8 million net increase in short-term borrowings partially offset by $32.2 million of capital expenditures.

The following table summarizes our cash flows for the fiscal year ended January 3, 2009, and December 29, 2007 ($ in millions):

	Fiscal Year Ended	
	January 3, 2009	December 29, 2007
Total cash provided by (used in):		
Operating activities	$ 3.0	$ 44.0
Investing activities	(32.2)	37.6

Financing activities	35.0	(83.1)
Increase (decrease) in cash and cash equivalents	$ 5.8	$ (1.5)

Cash provided by operating activities for the fiscal year ended January 3, 2009 and December 29, 2007 was $3.0 million and $44.0 million, respectively. The $41.1 million year-over-year decrease in cash from operating activities was comprised of a $97.8 million decline in net (loss) income and a $5.7 million decrease in cash from changes in operating assets and liabilities, partially offset by a $62.4 million increase in adjustments to reconcile net (loss) income to cash provided by operating activities, which was primarily due to the $34.0 million increase in disposals and impairments of assets and a $26.8 million deferred tax asset valuation allowance recorded in 2008. The year-over-year decrease in cash from changes in operating assets and liabilities was primarily due to a decrease in accounts payable (reduced inventory levels and reduced business volumes, partially offset by extended vendor payment terms) and an increase in income taxes receivables (tax benefit from pre-tax loss in current fiscal year), partially offset by a current-year decrease in inventories (inventories align with reduced sales volume), a current-year decrease in accounts receivable (lower 2008 sales volume), a current-year decrease in prepaid expenses and other assets, and a reduced current-year decrease in accrued compensation and benefits (prior-year's reduction included payment of fiscal 2006 annual incentive compensation in the first quarter of fiscal 2007).

Net cash used in investing activities was $32.2 million for 2008, compared with net cash provided by investing activities of $37.6 million for the same period one year ago. The $69.8 million decrease in net cash (used in) provided by investing activities was principally due to no proceeds from the sales and maturity of marketable debt securities for 2008, compared with $81.1 million of proceeds from the sales and maturity of marketable debt securities for the same period one year ago, as we liquidated our marketable debt securities in fiscal 2007 to fund common stock repurchases. During 2008, we invested $32.2 million in property and equipment, compared to $43.5 million for the same period one year ago. In both periods, our capital expenditures related primarily to new and remodeled retail stores, and investments in information technology. During 2008 we opened 19 new retail stores, compared with 45 new retail stores opened during the same period one year ago.

Net cash provided by financing activities was $35.0 million for 2008, compared with net cash used in financing activities of $83.1 million for the same period one year ago. The $118.2 million increase in cash provided by (used in) financing activities resulted from $134.5 million of common stock repurchases during 2007 compared with no repurchases for the fiscal 2008, partially offset by a $9.4 million net decrease in short-term borrowings compared with the prior year, a $3.9 million reduction in proceeds from the issuance of common stock related to stock option exercises and employee purchases, a $1.5 million reduction in tax benefits from stock-based compensation and a $1.5 million increase in debt issuance costs related to our amended credit agreement. Book overdrafts are included in the net change in short-term borrowings.

On April 20, 2007, our Board of Directors authorized us to repurchase up to an additional $250 million of our common stock, bringing the total availability under our share repurchase program to $290 million. In the third quarter of 2007, we curtailed our share repurchases following the tightening of credit markets and the continued deterioration in the general economic environment. During 2008 we did not purchase any shares of common stock compared with the purchase of 7.6 million shares of common stock at a total cost of $134.5 million (based on settlement dates) in 2007. As of January 3, 2009, the remaining authorization under our stock repurchase program was $206.8 million. There is no expiration date governing the period over which we can repurchase shares. We currently have no plans to repurchase our common stock.

In June 2006, we entered into a Credit Agreement (the "Credit Agreement") with a syndicate of banks (the "Lenders"). The Credit Agreement, as amended to date, provides a revolving credit facility in an aggregate amount of $90 million to be used for general corporate purposes (scheduled reductions in availability described below limit our borrowings plus outstanding letters of credit to $85 million as of March 31, 2009 and to $80 million as of July 1, 2009). The Credit Agreement terminates in June 2010.

The Credit Agreement was amended on February 1, 2008 and on May 30, 2008 to allow greater flexibility under the existing financial covenants, provide additional financial covenants and monthly measurement of financial covenants, modify the credit limit and maturity date, increase the cost of borrowing, provide the Lenders with a collateral security interest in substantially all of our assets and those of our subsidiaries, and impose additional restrictions and covenants with respect to our operations.

We had outstanding borrowings of $79.2 million and $37.9 million, under the credit facility as of January 3, 2009, and December 29, 2007, respectively. We also had outstanding letters of credit of $5.9 million and zero as of January 3, 2009, and December 29, 2007, respectively. Outstanding letters of credit reduce the amounts available under the credit facility. At January 3, 2009, and December 29, 2007, $5.0 million and $62.1 million, respectively, were available under this credit facility. In early March 2009, we received a federal income tax refund of approximately $23.0 million. Pursuant to the terms of the Credit Agreement, these funds have been placed in a cash collateral account with the Lenders. We are in discussions with the Lenders regarding the potential use or application of these funds to address our near-term liquidity needs.

At January 3, 2009, borrowings under the credit facility bore interest at a floating rate and could be maintained as base rate loans (tied to the prime rate, plus a margin of up to 4.00% or the federal funds rate plus 5.00%) or as Eurocurrency rate loans (tied to LIBOR, plus a margin up to 5.0% depending on our leverage ratio, as defined). We also pay certain facility and agent fees. As of January 3, 2009, and December 29, 2007, interest rates on borrowings outstanding under the Credit Agreement were 6.0% and 5.2%, respectively. We are subject to certain financial covenants under the agreement, including a maximum leverage ratio, a minimum interest coverage ratio, minimum EBITDA requirements and capital expenditure limits.

As of January 3, 2009, pursuant to an amendment of the Credit Agreement, the Lenders had waived compliance, through the close of business on January 15, 2009, with the Credit Agreement's financial covenants as of the end of fiscal year 2008. Pursuant to an amendment of the Credit Agreement entered into as of February 28, 2009, the Lenders waived compliance, through the close of business on March 30, 2009, with (a) the minimum interest coverage ratio covenant of the Credit Agreement for the fiscal periods ending on or about December 31, 2008, January 31, 2009 and February 28, 2009, and (b) the minimum EBITDA covenant of the Credit Agreement for the fiscal period ending on or about December 31, 2008. Upon expiration of our most recent amendment on March 31, 2009, we will not be in compliance with certain financial covenants under the Credit Agreement. If we are unable to continue to obtain amendments from the Lenders that waive compliance with these financial covenants, the Lenders could place us in default under the terms of the Credit Agreement.

We have taken significant actions to improve our operating results and maintain our liquidity in the current challenging macro-economic environment, including corporate workforce reductions, reduced capital spending, executing plans to close stores, supply chain cost reduction initiatives, reduced media spending, reductions in fixed and discretionary marketing and selling expenses, and ceasing all activities associated with the implementation of SAP®-based information technology applications. We recently introduced lower product price points and initiated an enhanced promotional strategy designed to stabilize sales. We have worked with our vendors to extend our payment terms and maintain positive working relationships. In addition, we are considering options to enhance our financial flexibility and fund our operations, including: additional actions to reduce our cost structure and improve profitability, the need to raise equity or debt capital, or the need to amend the financial covenants under our Credit Agreement. Any amendment of the Credit Agreement may significantly increase the cost of credit provided under the credit facility and related expenses, which may adversely impact our profitability. Whether or not we obtain an amendment of the Credit Agreement, we may need to or choose to seek additional capital through the issuance of debt or equity securities. The issuance of any additional debt securities could materially and adversely impact our profitability and financial condition. The issuance of additional equity securities could be substantially dilutive to our existing shareholders.

If we are unable to obtain additional capital, we may not be able to fund our operating needs and we could face a risk of default under our Credit Agreement. A default under the Credit Agreement would enable the Lenders to seek immediate payment in full of any amounts outstanding under the credit facility and to exercise various remedies as secured creditors, which may severely or completely constrain our ability to continue to operate our business as a going concern and may require us to seek protection from creditors through bankruptcy proceedings. Our uncertain financial position may also disrupt relationships with our suppliers. These conditions raise substantial doubt about our ability to continue as a going concern.

Our agreement under which GE Money Bank offers to our qualified customers revolving credit arrangements to finance purchases from us (the "GE Agreement") contains certain financial covenants, including maximum leverage ratio and minimum interest coverage. As our recent results placed us outside of these financial covenants, we were required under the terms of the GE Agreement to provide GE Money Bank with a $2.7 million letter of credit as collateral security.

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Outlook

We do not plan to provide specific earnings guidance for 2009. However, we have outlined our key business drivers and trends, which we believe will assist investors and analysts in understanding and analyzing our business.

We expect that macro-economic trends and consumer confidence will remain weak throughout 2009, and that our sales will decline commensurate with our peer group. As a result of the significant actions taken to reduce costs, we expect to achieve positive free cash flow and moderately improved profitability in the first quarter and full year 2009, (exclusive of the impact of asset impairments and other special charges incurred in 2008).

Sales assumptions for 2009 include the anticipated opening of 2 new stores and closing of 55 or more stores.

The company has taken actions to reduce 2009 fixed and discretionary costs by more than $80 million in addition to cost reduction and margin improvement actions in 2008 that aggregated to more than $40 million in fiscal 2008. Cost reductions in 2009 included the following:

- Product redesign and supply chain restructuring that we believe will reduce product costs by $16 million. We project our gross margin rate to be at or slightly lower than 2008 as product cost reductions will be offset by an increase in promotional activities.

- We plan to reduce media expenditures by approximately $30 million and reduce other fixed and discretionary sales and marketing costs by approximately $20 million. Planned store closures will reduce costs by approximately $10 million. Sales and marketing expenses are anticipated to decline by more than 200 basis points in 2009 on lower sales volume. We plan to manage our media investment as a variable cost to sales.

- We expect general and administrative expenses to be approximately $48 million in 2009, reflecting reductions in workforce and fixed G&A of approximately $10 million and before consideration of any incentive compensation expense that would be recorded if we exceed our earnings targets.

- Capital expenditures are expected to be reduced by $25 million or more in 2009.

Finally, we will continue to analyze our existing manufacturing, distribution and retail operations to optimize our business performance. As a result, in future periods, we may incur restructuring expenses or asset impairment charges.

Off-Balance Sheet Arrangements and Contractual Obligations

Other than our operating leases and $5.9 million of outstanding letters of credit, we do not have any off-balance-sheet financing. A summary of our operating lease obligations by fiscal year is included in the "Contractual Obligations" section below. Additional information regarding our operating leases is available in Item 2, *Properties*, and Note 4, *Leases*, of the Notes to Consolidated Financial Statements, included in Item 8, *Financial Statements and Supplementary Data*, of this Annual Report on Form 10-K.

Contractual Obligations

The following table presents information regarding our contractual obligations by fiscal year (in thousands):

	Payments Due by Period(1)				
	Total	**< 1 Year**	**1 – 3 Years**	**3 – 5 Years**	**> 5 Years**
Short-term debt obligations	$ 79,150	$ 79,150	$ —	$ —	$ —
Operating leases	157,889	34,540	58,931	39,401	25,017
Capital leases	845	302	543	—	—
Purchase commitments	159,200	64,200	95,000	—	—
Total	$ 397,084	$ 178,192	$ 154,474	$ 39,401	$ 25,017

(1) Our unrecognized tax benefits of $155,000 have not been included in the Contractual Obligations table as we are not able to determine a reasonable estimate of timing of the cash settlement with the respective taxing authorities.

Critical Accounting Policies and Estimates

Our consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). In connection with the preparation of our financial statements, we are required to make estimates and assumptions about future events, and apply judgments that affect the reported amounts of assets, liabilities, sales, expenses and the related disclosure. 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. We base our assumptions, estimates and judgments on historical experience, current trends and other factors that management believes to be relevant at the time our consolidated financial statements are prepared. On a regular basis, management reviews the accounting policies, assumptions, estimates and judgments to ensure that our financial statements are presented fairly and in accordance with GAAP. However, because future events and their effects cannot be determined with certainty, actual results could differ from our assumptions and estimates, and such differences could be material.

Our significant accounting policies are discussed in Note 1, *Business and Summary of Significant Accounting Policies*, of the Notes to Consolidated Financial Statements, included in Item 8, *Financial Statements and Supplementary Data*, of this Annual Report on Form 10-K. Management believes the accounting policies discussed below are the most critical because they require management's most difficult, subjective or complex judgments, resulting from the need to make estimates about the effect of matters that are inherently uncertain. Management has reviewed these critical accounting policies and estimates and related disclosures with the Audit Committee of our Board.

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Our critical accounting policies and estimates relate to asset impairment charges, stock-based compensation, deferred income taxes, self-insured liabilities, warranty liabilities and revenue recognition.

Description	Judgments and Uncertainties	Effect if Actual Results Differ From Assumptions
Asset Impairment Charges		
Long-lived assets other than goodwill and other intangible assets, which are separately tested for impairment, are evaluated for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We evaluate our long-lived assets for impairment based on estimated future cash flows after considering the potential impact of planned operational improvements, marketing programs, industry economic factors and the profitability of future business strategies. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted cash flows expected to be generated by the asset plus net proceeds expected from disposition of the asset (if any). When we recognize an impairment loss, the carrying amount of the asset is reduced to estimated fair value based on discounted cash flows, quoted market prices or other valuation techniques. Assets to be disposed of are reported at the lower of the carrying amount of the asset or fair value less costs to sell. We review store assets for potential impairment based on historical cash flows, lease termination provisions and expected future store operating results. If we recognize an impairment loss, the adjusted carrying amount of the asset becomes its new cost basis. For a depreciable long-lived asset, the new cost basis will be depreciated (amortized) over the remaining useful life of that asset. Asset impairment charges totaled $34,594,000, $409,000 and $5,980,000, respectively, for 2008, 2007 and 2006.	Our impairment loss calculations contain uncertainties because they require management to make assumptions and to apply judgment to identify events or changes in circumstances indicating the carrying value of assets may not be recoverable, estimate future cash flows, estimate asset fair values, and select a discount rate that reflects the risk inherent in future cash flows. 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.	We have not made any material changes in our impairment loss assessment methodology during the past three fiscal years. We believe that our estimates and assumptions used to calculate long-lived asset impairment charges were reasonable and reflect the current economic environment. However, it is reasonably possible that a prolonged economic slowdown or further deterioration of consumer spending may expose us to future impairment charges that could be material. Alternatively, if consumer spending increases at a higher rate than we anticipated, impaired stores (which continue to operate) could generate higher than expected future cash flows and operating profits.

Description	Judgments and Uncertainties	Effect if Actual Results Differ From Assumptions
Stock-Based Compensation		
We have a stock-based compensation plan, which includes non-qualified stock options and nonvested share awards, and an employee stock purchase plan. See Note 1, *Business and Summary of Significant Accounting Policies*, and Note 7, *Shareholders' Equity*, to the Notes to Consolidated Financial Statements, included in Item 8, *Financial Statements and Supplementary Data*, of this Annual Report on Form 10-K, for a complete discussion of our stock-based compensation programs. We determine the fair value of our non-qualified stock option awards and the resulting compensation expense at the date of grant using the Black-Scholes-Merton option-pricing model. The most significant inputs into the Black-Scholes-Merton model are exercise price, our estimate of expected stock price volatility and the expected term of the options. Previously, two alternative methods existed for accounting for stock options: the intrinsic value method and the fair value method. Prior to fiscal 2006, we used the intrinsic value method of accounting for stock options and under that standard, no compensation expense was recognized in the financial statements for options granted to employees, or for the discount feature of our employee stock purchase plan. We determine the fair value of our performance-based nonvested share awards at the date of grant using generally accepted valuation techniques and the closing market price of our stock.	Option-pricing models and generally accepted valuation techniques require management to make assumptions and to apply judgment to determine the fair value of our awards. These assumptions and judgments include estimating the future volatility of our stock price, future employee forfeiture rates and future employee stock option exercise behaviors. Changes in these assumptions can materially affect the fair value estimate or future earnings adjustments. Performance-based nonvested share awards require management to make assumptions regarding the likelihood of achieving personal performance goals.	We do not believe there is a reasonable likelihood that there will be a material change in the future estimates or assumptions we use to determine stock-based compensation expense. However, if actual results are not consistent with our estimates or assumptions, we may be exposed to changes in stock-based compensation expense that could be material. If actual results are not consistent with the assumptions used, the stock-based compensation expense reported in our financial statements may not be representative of the actual economic cost of the stock-based compensation. Also, if the actual forfeiture rates are not consistent with the assumptions used, it could result in future earnings adjustments. A 10% change in our stock-based compensation expense for the year ended January 3, 2009, would have affected net income by approximately $220,000 in 2008.

Description	Judgments and Uncertainties	Effect if Actual Results Differ From Assumptions
Deferred Income Taxes		
We recognize deferred tax assets and liabilities for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Realization of deferred tax assets is dependent on generating sufficient taxable income within the carryback or carryforward periods provided for in the tax law of each applicable tax jurisdiction. We establish a valuation allowance for any portion of deferred tax assets that are not considered more likely than not to be realized. Our evaluation includes a review of the future reversal of existing taxable temporary differences, future taxable income, taxable income available in carryback periods and tax	Our deferred tax valuation allowance contains uncertainties because it requires management to consider all available evidence, both positive and negative, including past operating results and apply judgment on our ability to generate future taxable income sufficient to realize our deferred tax assets. From 2002 through 2007, we generated income before income taxes on average of $50.6 million. Our 2008 operating results were significantly affected by the industry-wide decrease in consumer spending and we realized a loss before income taxes of $72.7 million, including $34.6 million of asset impairment charges. Determining that a valuation allowance is not required is difficult to overcome when there is negative evidence which is objective and verifiable, including our significant net loss in the current year. In addition, while our long-term outlook is positive, we expect macro-economic trends and consumer confidence to	We have not made any material changes in our deferred tax assessment methodology during the past three fiscal years. If and when our operating performance improves on a sustained basis, our conclusion regarding the need for a $26.8 million deferred tax valuation allowance could change, resulting in the reversal of some or all of the valuation allowance in future periods.

planning strategies.

Our net deferred tax assets, prior to the valuation allowance, totaled $34.2 million and $32.4 million, respectively, for 2008 and 2007.

remain weak throughout 2009, further pressuring our operating results. Thus, we concluded that our ability to rely on our long-term outlook in generating future taxable income was limited due to uncertainty created by our 2008 loss and the weak 2009 macro-economic outlook.

Based on the significant change in the economic environment in the fourth quarter of 2008 and the discussion above, we recorded a $26.8 million charge for deferred tax assets that could not be realized through taxable income earned in available carryback periods. The $26.8 million charge establishes a valuation allowance against deferred tax assets that are not considered more likely than not to be realized.

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Description	Judgments and Uncertainties	Effect if Actual Results Differ From Assumptions
Self-Insured Liabilities		
We are self-insured for certain losses related to health and workers' compensation claims. However, we obtain third-party insurance coverage to limit our exposure to these claims. When estimating our self-insured liabilities, we consider a number of factors, including historical claims experience, demographic factors, severity factors and valuations provided by third-party administrators. Periodically, management reviews its assumptions and the valuations provided by third-party administrators to determine the adequacy of our self-insured liabilities.	Our self-insured liabilities contain uncertainties because management is required to make assumptions and to apply judgment to estimate the ultimate cost to settle reported claims and claims incurred but not reported as of the balance sheet date.	We have not made any material changes in the accounting methodology used to establish our self-insured liabilities during the past three fiscal years. We do not believe there is a reasonable likelihood that there will be a material change in the estimates or assumptions we use to calculate our self-insured liabilities. However, if actual results are not consistent with our estimates or assumptions, we may be exposed to losses or gains that could be material. A 10% change in our self-insured liabilities at January 3, 2009, would have affected net income by approximately $284,000 in 2008.
Warranty Liabilities		
The estimated cost to service warranty claims of customers is included in cost of sales. This estimate is based on historical trends of warranty claims. We regularly assess and adjust the estimate of accrued warranty claims by updating claims rates for actual trends and projected claim costs.	Our warranty liability contains uncertainties because our warranty obligations cover an extended period of time. A revision of estimated claim rates or the projected cost of materials and freight associated with sending replacement parts to customers could have a material adverse effect on future results of operations.	We do not believe there is a reasonable likelihood that there will be a material change in the estimates or assumptions we use to calculate our warranty liability. However, if actual results are not consistent with our estimates or assumptions, we may be exposed to losses or gains that could be material. A 10% change in our warranty liability at January 3, 2009, would have affected net income by approximately $478,000 in 2008.
Revenue Recognition		
Revenue is recognized when the sales price is fixed or determinable, collectability is reasonably assured and title passes. Amounts billed to customers for delivery and set up are included in net sales. Revenue is reported net of estimated sales returns and excludes sales taxes. We accrue for sales returns at the time revenue is recognized and charge actual returns against the liability when they are received. Our general return policy is to allow returns for up to 30 nights following a sale. We estimate future projected returns based on historical return rates.	Our estimates of sales returns contains uncertainties as actual returns may vary from expected rates, resulting in adjustments to net sales in future periods. These adjustments could have a material adverse effect on future results of operations.	We have not made any material changes in the accounting methodology used to establish our sales returns allowance during the past three fiscal years. We do not believe there is a reasonable likelihood that there will be a material change in the estimates or assumptions we use to calculate our sales returns allowance. However, if actual results are not consistent with our estimates or assumptions, we may be exposed to losses or gains that could be material. A 10% change in our sales returns allowance at January 3, 2009, would have affected net income by approximately $163,000 in 2008.

Recent Accounting Pronouncements

In February 2008, the FASB issued Financial Staff Position ("FSP") No. 157-2, *Effective Date of FASB Statement No. 157*, which delays the effective date of SFAS No. 157 ("FSP 157-2") for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). SFAS No. 157 establishes a framework for measuring fair value and expands disclosures about fair value measurements. FSP 157-2 partially defers the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of this FSP. The adoption of SFAS No. 157 for all nonfinancial assets and nonfinancial liabilities is effective for us beginning January 4, 2009. We do not expect the adoption of FSP 157-2 to have a material impact on our consolidated financial statements.

In April 2008, the FASB issued FSP No. 142-3, *Determination of the Useful Life of Intangible Assets* ("FSP 142-3"). FSP 142-3 amends the factors to be considered in developing renewal or extension assumptions used to determine the useful life of intangible assets under SFAS No. 142, "Goodwill and Other Intangible Assets." Its intent is to improve the consistency between the useful life of an intangible asset and the period of expected cash flows used to measure its fair value. This FSP is effective prospectively for intangible assets acquired or renewed after January 1, 2009. We do not expect FSP 142-3 to have a material impact on our consolidated financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

At January 3, 2009, our short-term debt was comprised primarily of borrowings under our revolving line of credit. We do not currently manage interest rate risk on our debt through the use of derivative instruments.

Borrowings under our revolving credit facility are currently not subject to material interest rate risk. The credit facility's interest rate may be reset due to fluctuations in a market-based index, such as the prime rate, federal funds rate or LIBOR. A hypothetical 100 basis point change in the interest rate on outstanding borrowings under our credit facility as of January 3, 2009 would change our annual consolidated pre-tax income by $0.8 million.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Select Comfort Corporation:

We have audited Select Comfort Corporation's internal control over financial reporting as of January 3, 2009, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Select Comfort Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting appearing under Item 9A of this Form 10-K. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Select Comfort Corporation maintained, in all material respects, effective internal control over financial reporting as of January 3, 2009, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Select Comfort Corporation and subsidiaries as of January 3, 2009 and December 29, 2007, and the related consolidated statements of operations, shareholders' (deficit) equity, and cash flows for each of the fiscal years in the three-year period ended January 3, 2009, and our report dated March 19, 2009 expressed an unqualified opinion on those consolidated financial statements. Our report on the consolidated financial statements included an explanatory paragraph related to the existence of substantial doubt as to the Company's ability to continue as a going concern.

KPMG LLP

Minneapolis, Minnesota
March 19, 2009

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Select Comfort Corporation:

We have audited the accompanying consolidated balance sheets of Select Comfort Corporation and subsidiaries (the Company) as of January 3, 2009 and December 29, 2007, and the related consolidated statements of operations, shareholders' (deficit) equity, and cash flows for each of the fiscal years in the three-year period ended January 3, 2009. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule, as listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Select Comfort Corporation and subsidiaries as of January 3, 2009 and December 29, 2007, and the results of their operations and their cash flows for each of the fiscal years in the three-year period ended January 3, 2009, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company's losses from operations and inability to generate sufficient cash flow to meet obligations and sustain operations raises substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

As described in Note 1 to the consolidated financial statements, the Company adopted the provisions of SFAS 157, *Fair Value Measurements*, and SFAS 159, *The Fair Value Option for Financial Assets and Liabilities*, on December 30, 2007 and FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, on December 31, 2006.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Select Comfort Corporation and subsidiaries' internal control over financial reporting as of January 3, 2009, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 19, 2009 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

KPMG LLP

Minneapolis, Minnesota
March 19, 2009

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SELECT COMFORT CORPORATION
AND SUBSIDIARIES

Consolidated Balance Sheets
January 3, 2009 and December 29, 2007
(in thousands, except per share amounts)

	2008	2007
Assets		
Current assets:		
Cash and cash equivalents	$ 13,057	$ 7,279
Accounts receivable, net of allowance for doubtful accounts of $713 and $876, respectively	4,939	18,902
Inventories	18,675	32,517
Income taxes receivable	25,900	—
Prepaid expenses	4,109	9,816
Deferred income taxes	1,323	6,796
Other current assets	1,150	3,833
Total current assets	69,153	79,143
Property and equipment, net	53,274	80,409
Deferred income taxes	5,941	25,543
Other assets	7,045	5,394
Total assets	$ 135,413	$ 190,489

Liabilities and Shareholders' (Deficit) Equity		
Current liabilities:		
Borrowings under revolving credit facility	$ 79,150	$ 37,890
Accounts payable	40,274	69,775
Customer prepayments	11,480	8,327
Accruals:		
Sales returns	2,744	3,751
Compensation and benefits	14,575	14,865
Taxes and withholding	2,938	4,812
Other current liabilities	8,526	9,723
Total current liabilities	159,687	149,143
Warranty liabilities	5,956	6,747
Capital lease obligations	621	—
Other long-term liabilities	10,779	10,473
Total non-current liabilities	17,356	17,220
Total liabilities	177,043	166,363
Shareholders' (deficit) equity:		
Undesignated preferred stock; 5,000 shares authorized, no shares issued and outstanding	—	—
Common stock, $0.01 par value; 142,500 shares authorized, 44,962 and 44,597 shares issued and outstanding, respectively	450	446
Additional paid-in capital	4,417	—
(Accumulated deficit) retained earnings	(46,497)	23,680
Total shareholders' (deficit) equity	(41,630)	24,126
Total liabilities and shareholders' (deficit) equity	$ 135,413	$ 190,489

See accompanying notes to consolidated financial statements.

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SELECT COMFORT CORPORATION
AND SUBSIDIARIES

Consolidated Statements of Operations
Years ended January 3, 2009, December 29, 2007 and December 30, 2006
(in thousands, except per share amounts)

	2008	2007	2006
Net sales	$ 608,524	$ 799,242	$ 806,038
Cost of sales	249,952	312,827	315,530
Gross profit	358,572	486,415	490,508
Operating expenses:			
Sales and marketing	332,068	372,467	341,630
General and administrative	57,994	64,351	65,401
Research and development	3,374	5,682	4,687
Asset impairment charges	34,594	409	5,980
Total operating expenses	428,030	442,909	417,698
Operating (loss) income	(69,458)	43,506	72,810
Other (expense) income, net	(3,285)	(40)	3,018
(Loss) income before income taxes	(72,743)	43,466	75,828
Income tax (benefit) expense	(2,566)	15,846	28,645
Net (loss) income	$ (70,177)	$ 27,620	$ 47,183
Basic net (loss) income per share:			
Net (loss) income per share – basic	$ (1.59)	$ 0.59	$ 0.89
Weighted-average common shares – basic	44,186	46,536	52,837
Diluted net (loss) income per share:			
Net (loss) income per share – diluted	$ (1.59)	$ 0.57	$ 0.85
Weighted-average common shares – diluted	44,186	48,292	55,587

See accompanying notes to consolidated financial statements.

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SELECT COMFORT CORPORATION
AND SUBSIDIARIES

Consolidated Statements of Shareholders' (Deficit) Equity
Years ended January 3, 2009, December 29, 2007 and December 30, 2006
(in thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings/ (Accumulated Deficit)	Total
Balance at December 31, 2005	53,598	536	56,854	63,957	121,347
Exercise of common stock options	1,544	15	7,495	—	7,510
Exercise of common stock warrants	75	1	—	—	1
Tax benefit from stock-based compensation	—	—	9,769	—	9,769
Stock-based compensation	—	—	8,325	—	8,325
Repurchases of common stock	(3,889)	(39)	(79,700)	—	(79,739)
Issuances of common stock	216	2	1,296	—	1,298
Net income	—	—	—	47,183	47,183
Balance at December 30, 2006	51,544	515	4,039	111,140	115,694
Exercise of common stock options	566	6	3,483	—	3,489
Tax benefit from stock-based compensation	—	—	1,887	—	1,887
Stock-based compensation	—	—	6,252	—	6,252
Repurchases of common stock	(7,617)	(76)	(16,756)	(115,080)	(131,912)
Issuances of common stock	104	1	1,095	—	1,096
Net income	—	—	—	27,620	27,620
Balance at December 29, 2007	44,597	$ 446	$ —	$ 23,680	$ 24,126
Exercise of common stock options	61	1	92	—	93
Tax benefit from stock-based compensation	—	—	28	—	28
Stock-based compensation	—	—	3,702	—	3,702
Issuances of common stock	304	3	595	—	598
Net loss	—	—	—	(70,177)	(70,177)
Balance at January 3, 2009	44,962	$ 450	$ 4,417	$ (46,497)	$ (41,630)

See accompanying notes to consolidated financial statements.

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SELECT COMFORT CORPORATION
AND SUBSIDIARIES

Consolidated Statements of Cash Flows
Years ended January 3, 2009, December 29, 2007 and December 30, 2006
(in thousands)

	2008	2007	2006
Cash flows from operating activities:			
Net (loss) income	$ (70,177)	$ 27,620	$ 47,183
Adjustments to reconcile net (loss) income to net cash provided by operating activities:			
Depreciation and amortization	22,186	24,791	19,752
Stock-based compensation	3,702	6,252	8,325
Disposals and impairments of assets	34,577	596	5,912
Excess tax benefits from stock-based compensation	(19)	(1,497)	(8,565)
Changes in deferred income taxes	25,075	(7,280)	(7,665)
Other, net	—	270	(68)
Change in operating assets and liabilities:			
Accounts receivable	13,963	(6,738)	(5,930)
Inventories	13,842	(8,397)	(2,138)
Income taxes receivable	(25,900)	—	—
Prepaid expenses and other assets	7,627	(1,020)	(823)
Accounts payable	(20,047)	12,201	6,091
Customer prepayments	3,153	(1,225)	(5,166)
Accrued sales returns	(1,007)	(156)	(1,496)
Accrued compensation and benefits	(250)	(5,179)	(4,782)
Accrued taxes and withholding	(1,846)	1,646	5,198
Warranty liabilities	(1,454)	(719)	2,574
Other accruals and liabilities	(452)	2,866	974
Net cash provided by operating activities	2,973	44,031	59,376
Cash flows from investing activities:			
Purchases of property and equipment	(32,202)	(43,514)	(31,079)
Investments in marketable debt securities	—	—	(28,072)
Proceeds from sales and maturity of marketable debt securities	—	81,086	25,940
Net cash (used in) provided by investing activities	(32,202)	37,572	(33,211)
Cash flows from financing activities:			

Net increase (decrease) in short-term borrowings	35,809	45,240	(1,388)
Repurchases of common stock	—	(134,452)	(77,199)
Proceeds from issuance of common stock	651	4,572	8,809
Debt issuance costs	(1,472)	—	—
Excess tax benefits from stock-based compensation	19	1,497	8,565
Net cash provided by (used in) financing activities	35,007	(83,143)	(61,213)
Increase (decrease) in cash and cash equivalents	5,778	(1,540)	(35,048)
Cash and cash equivalents, at beginning of year	7,279	8,819	43,867
Cash and cash equivalents, at end of year	$ 13,057	$ 7,279	$ 8,819
Supplemental Disclosure of Cash Flow Information			
Income taxes (refunded) paid	$ (1,313)	$ 20,622	$ 30,628
Interest paid	$ 3,636	$ 1,095	$ —
Capital lease obligations incurred	$ 1,032	$ —	$ —
Purchases of property and equipment included in accounts payable	$ 770	$ 4,960	$ 2,098

See accompanying notes to consolidated financial statements.

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(1) Business and Summary of Significant Accounting Policies

Business

Select Comfort Corporation and our wholly-owned subsidiaries ("Select Comfort" or the "Company") develops, manufactures and markets premium quality, adjustable-firmness beds and related bedding accessories in the United States. In addition, we also sell to wholesale customers in Canada and Australia. We sell through four distribution channels: Retail, Direct, E-Commerce and Wholesale. The percentage of our total net sales from each of our channels during the last three years was as follows:

	2008	2007	2006
Retail	78.2%	75.4%	76.2%
Direct	7.7%	8.0%	9.4%
E-Commerce	6.1%	6.8%	5.6%
Wholesale	8.0%	9.8%	8.8%
Total	100.0%	100.0%	100.0%

Basis of Presentation, Liquidity and Going Concern

The consolidated financial statements include the accounts of Select Comfort Corporation and our subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

In 2008, following several years of generating positive net income, we realized a net loss of $70.2 million, including $34.6 million of asset impairment charges and a $26.8 million charge for the establishment of a deferred tax valuation allowance. Our 2008 operating results were significantly affected by an industry-wide decrease in consumer spending. While we generated $3.0 million of operating cash flows in 2008, the decline in our operating performance and the acceleration of the decline of consumer demand in the fourth quarter of 2008 has affected our liquidity.

As of January 3, 2009, we had outstanding borrowings of $79.2 million, plus $5.9 million under letters of credit, with an additional $5.0 million available under our $90 million credit facility. Pursuant to a series of amendments of our Credit Agreement, the Lenders have deferred to March 31, 2009 a reduction in the amount available under our line of credit from $90 million to $85 million that was previously scheduled to become effective as of December 1, 2008. Also pursuant to these amendments, the Lenders have waived compliance, through the close of business on March 30, 2009, with certain financial covenants under the Credit Agreement applicable to fiscal periods ending on or about December 31, 2008, January 31, 2009 and February 28, 2009. In early March 2009, we received a federal income tax refund of approximately $23.0 million. Pursuant to the terms of the Credit Agreement, these funds have been placed in a cash collateral account with the Lenders. Upon expiration of our most recent amendment on March 30, 2009, we will not be in compliance with certain financial covenants under the credit agreement. If we are unable to continue to obtain amendments from the Lenders that waive compliance with these financial covenants, the Lenders could place us in default under terms of our credit agreement. Even if we obtain amendments to our credit agreement, our business may require additional capital in order to fund our operating needs. A default under the Credit Agreement would enable the Lenders to seek immediate payment in full of any amounts outstanding under the credit facility and to exercise various remedies as secured creditors, which may severely or completely constrain our ability to continue to operate our business and may require us to seek protection from creditors through bankruptcy proceedings. Our uncertain financial position may also disrupt relationships with our suppliers.

We expect macro-economic trends and consumer confidence to remain weak throughout 2009. We have taken significant actions designed to return the company to profitability and generate positive cash flows to fund our business, including: corporate workforce reductions, reduced capital spending, development of plans to close stores, supply chain cost reduction initiatives, reduced media spending, reductions in fixed and discretionary marketing and selling expenses, and ceasing all activities associated with the implementation of SAP®-based information technology applications. We recently introduced lower product price points and initiated an enhanced promotional strategy designed to stabilize sales. However, further expense reductions may be necessary should our 2009 net sales decline at a steeper rate than we currently expect. In addition to actions to align our cost structure with expected sales declines, we have been exploring a range of strategic and financing alternatives to enhance our financial flexibility.

Our ability to continue as a going concern is dependent on various factors, including: macro economic trends, the successful execution of our cost reduction plans, successful negotiation with the Lenders and successful efforts to raise additional capital. Some of these factors are not entirely within our control. These conditions raise substantial doubt about our ability to continue as a going concern.

Our financial statements have been prepared on the going concern basis, which assumes the realization of assets and liquidation of liabilities in the normal course of operations. The consolidated financial statement do not include any adjustments relating to the recoverability or classification of recorded asset amounts or the amounts or classification of liabilities should we be unable to continue as a going concern.

Fiscal Year

Our fiscal year ends on the Saturday closest to December 31. Fiscal years and their respective fiscal year ends are as follows: fiscal 2008 ended January 3, 2009; fiscal 2007 ended December 29, 2007; and fiscal year 2006 ended December 30, 2006. Fiscal 2008 had 53 weeks. Fiscal years 2007 and 2006 each had 52 weeks.

Use of Estimates in the Preparation of Financial Statements

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles (“GAAP”) requires us to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of sales and expenses during the reporting period. Predicting future events is inherently an imprecise activity and, as such, requires the use of judgment. Illiquid credit markets and declines in consumer spending have combined to increase the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods. Our critical accounting policies consist of asset impairment charges, stock-based compensation, deferred income taxes, self-insured liabilities, warranty liabilities and revenue recognition.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with original maturities of three months or less. Outstanding checks in excess of funds on deposit (“book overdrafts”) totaled $11.7 million and $17.0 million at January 3, 2009, and December 29, 2007, respectively. Book overdrafts are included in accounts payable in our consolidated balance sheets and in financing activities in our consolidated statements of cash flows.

The majority of payments due from third-parties for credit card and debit card transactions are processed within one to three business days. All credit card and debit card transactions that process in less than seven days are classified as cash and cash equivalents. Amounts due for these transactions that are classified as cash and cash equivalents totaled $2.1 million and $4.9 million at January 3, 2009, and December 29, 2007, respectively.

Accounts Receivable

Accounts receivable are recorded net of an allowance for expected losses and consist primarily of wholesale receivables and receivables from third-party financiers for customer credit card purchases. The allowance is recognized in an amount equal to anticipated future write-offs. We estimate future write-offs based on delinquencies, aging trends, industry risk trends and our historical experience.

Marketable Debt Securities

Marketable debt securities included highly liquid investment grade debt instruments with original maturities of greater than 90 days issued by the U.S. government and related agencies and municipalities. We did not hold any marketable debt securities at January 3, 2009, or December 29, 2007.

Investments held had an original maturity of up to 36 months. Marketable debt securities with a remaining maturity of greater than one year were classified as non-current.

Through December 30, 2006, we classified our marketable debt securities as “held-to-maturity” in accordance with Financial Accounting Standards Board (“FASB”) Statement of Financial Accounting Standards (“SFAS”) No. 115, “*Accounting for Certain Investments in Debt and Equity Securities.*” We historically valued our marketable debt securities at amortized cost

based upon our intent and ability to hold these securities to maturity. On March 23, 2007, marketable debt securities of $67.8 million with an unrealized net loss of $0.3 million were transferred from “held-to-maturity” classification to “available-for-sale” classification. Investments classified as “available-for-sale” are carried at fair market value. The classification change was made to increase liquidity and fund our common stock repurchase program.

During 2007, marketable debt securities with a cost of $64.4 million were sold at a realized loss of $0.3 million. Realized gains and losses are included in other (expense) income, net in our consolidated statements of operations.

Inventories

Inventories include material, labor and overhead and are stated at the lower of cost or market. Cost is determined by the first-in, first-out method.

Property and Equipment

Property and equipment, carried at cost, is depreciated using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are depreciated over the shorter of the estimated useful lives of the assets or the contractual term of the lease, with consideration of lease renewal options if renewal appears probable. Property under capital lease is comprised of manufacturing equipment, and computer equipment used in our retail operations and corporate support areas. Estimated useful lives of our property and equipment by major asset category are as follows:

Leasehold improvements	5 to 10 years
Office furniture and equipment	5 to 7 years
Production machinery, computer equipment and software	3 to 7 years
Property under capital lease	3 to 4 years

Other Assets

Other assets include deposits, patents, trademarks and goodwill. Patents and trademarks are amortized using the straight-line method over periods ranging from 10 to 17 years. The carrying value of goodwill at both January 3, 2009, and December 29, 2007, was $2.9 million.

Asset Impairment Charges

We review our long-lived assets and identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted cash flows expected to be generated by the asset plus net proceeds expected from disposition of the asset (if any). When we recognize an impairment loss, the carrying amount of the asset is reduced to estimated fair value based on discounted cash flows, quoted market prices or other valuation techniques. Assets to be disposed of are reported at the lower of the carrying amount of the asset or fair value less costs to sell. We review store assets for potential impairment based on historical cash flows, lease termination provisions and expected future store operating results.

The test for goodwill impairment is a two-step process, and is performed at least annually. The first step is a comparison of the fair value of the reporting unit with its carrying amount, including goodwill. If this step reflects impairment, then the loss would be measured as the excess of recorded goodwill over its implied fair value. Implied fair value is the excess of fair value of the reporting unit over the fair value of all identified assets and liabilities. Fair value is determined utilizing widely accepted valuation techniques, including quoted market prices and our market capitalization. During the fourth quarter of 2008, we completed our annual impairment testing of goodwill, using the valuation techniques as described above, and determined there was no impairment.

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Warranty Liabilities

We provide a 20-year limited warranty on our adjustable-firmness beds. The customer participates over the last 18 years of the warranty period by paying a portion of the retail value of replacement parts. Estimated warranty costs are expensed at the time of sale based on historical claims rates incurred by us and are adjusted for any current trends as appropriate. Actual warranty claim costs could differ from these estimates. We classify as noncurrent those estimated warranty costs expected to be paid out in greater than one year. The activity in the accrued warranty liabilities account was as follows (in thousands):

	Balance at Beginning of Year	Additions Charged to Costs and Expenses	Deductions from Reserves	Balance at End of Year
2008	$ 9,503	$ 8,083	$ 9,537	$ 8,049
2007	10,223	10,373	11,093	9,503
2006	7,649	13,521	10,947	10,223

Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, accounts receivable, accounts payable, borrowings under our revolving credit facility, and other current assets and liabilities approximate fair value because of their short-term maturity.

We adopted the provisions of SFAS No. 157, "*Fair Value Measurements*" on December 30, 2007, the beginning of our 2008 fiscal year. SFAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements are separately disclosed by level within the fair value hierarchy. SFAS No. 157, as originally issued, was effective for fiscal years beginning after November 15, 2007, with early adoption permitted. However, on February 12, 2008, the FASB issued FASB Staff Position ("FSP") FAS 157-2, which deferred the effective date of SFAS No. 157 for one year, as it relates to nonfinancial assets and liabilities. Accordingly, our adoption related only to financial assets and liabilities. At January 3, 2009, and December 29, 2007, we had no financial assets or liabilities which required a fair value measurement on a recurring basis. The adoption of this statement had no impact on our consolidated financial statements.

We adopted the provisions of SFAS No. 159, "*The Fair Value Option for Financial Assets and Liabilities – Including an Amendment of FASB Statement No. 115*" on December 30, 2007, the beginning of our 2008 fiscal year. SFAS No. 159 permits us to choose to measure certain financial assets and liabilities at fair value that are not currently required to be measured at fair value (the "Fair Value Option"). Election of the Fair Value Option is made on an instrument-by-instrument basis and is irrevocable. At the adoption date, unrealized gains and losses on financial assets and liabilities for which the Fair Value Option has been elected are reported as a cumulative adjustment to beginning retained earnings. We did not elect the Fair Value Option as we had no financial assets or liabilities that qualified for this treatment. In the future, if we elect the Fair Value Option for certain financial assets and liabilities, we would report unrealized gains and losses due to changes in their fair value in net income at each subsequent reporting date. The adoption of this statement had no impact on our consolidated financial statements.

Revenue Recognition

Revenue is recognized when the sales price is fixed or determinable, collectability is reasonably assured and title passes. Amounts billed to customers for delivery and set up are included in net sales. Revenue is reported net of estimated sales returns and excludes sales taxes.

We accept sales returns up to 30 nights following the sale. The accrued sales returns estimate is based on historical return rates, which are reasonably consistent from period to period and is adjusted for any current trends as appropriate. If actual returns vary from expected rates, sales in future periods are adjusted.

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Notes to Consolidated Financial Statements – (continued)

Cost of Sales, Sales and Marketing, General and Administrative ("G&A") and Research & Development ("R&D") Expenses

The following tables summarize the primary costs classified in each major expense category (the classification of which may vary within our industry):

Cost of Sales

- Costs associated with purchasing, manufacturing, shipping, handling and delivering our products to our stores and customers;
- Physical inventory losses, scrap and obsolescence;
- Related occupancy and depreciation expenses; and
- Estimated costs to service warranty claims of customers.

Sales & Marketing

- Advertising and media production;
- Marketing and selling materials such as brochures, videos, customer mailings and in-store signage;
- Payroll and benefits for sales and customer service staff;
- Store occupancy costs;
- Store depreciation expense; and
- Promotional financing costs.

G&A

- Payroll and benefit costs for corporate employees, including information technology, legal, human resources, finance, sales and marketing administration, investor relations and risk management;
- Occupancy costs of corporate facilities;
- Depreciation related to corporate assets;
- Information hardware, software and maintenance;
- Insurance;
- Investor relations costs; and
- Other overhead costs.

R&D[(1)]

- Internal labor and benefits related to research and development activities;
- Outside consulting services related to research and development activities; and
- Testing equipment related to research and development activities.

(1) Costs incurred in connection with R&D are charged to expense as incurred.

Operating Leases

We rent office and manufacturing space under operating leases which, in addition to the minimum lease payments, require payment of a proportionate share of the real estate taxes and certain building operating expenses. We also rent retail space under operating leases which, in addition to the minimum lease payments, may require payment of contingent rents based upon sales levels and payment of a proportionate share of the real estate taxes and certain building operating expenses.

Rent expense is recognized on a straight-line basis over the lease term, after consideration of rent escalations and rent holidays. We record any difference between the straight-line rent amounts and amounts payable under the leases as part of deferred rent, in other current liabilities or other long-term liabilities, as appropriate. The lease term for purposes of the calculation begins on the earlier of the lease commencement date or the date we take possession of the property. At January 3, 2009, and December 29, 2007, deferred rent included in other current liabilities in our consolidated balance sheets was $1.3 million and $0.2 million, respectively, and deferred rent included in other long-term liabilities in our consolidated balance sheets was $4.3 million and $4.7 million, respectively.

Leasehold improvements that are funded by landlord incentives or allowances under an operating lease are recorded as deferred rent, in other current liabilities or other long-term liabilities, as appropriate and amortized as reductions to rent expense over the lease term.

Lease payments that depend on factors that are not measurable at the inception of the lease, such as future sales levels, are contingent rents and are excluded from minimum lease payments and included in the determination of total rent expense when it is probable the expense has been incurred and the amount is reasonably estimable. Future payments for real estate taxes and certain building operating expenses for which we are obligated are not included in minimum lease payments.

We also lease delivery trucks associated with our home delivery service, which in addition to the minimum lease payments, require payment of a management fee and contain certain residual value guarantee provisions that would become due at the expiration of the operating agreement if the fair value of the leased vehicles is less than the guaranteed residual value. As of January 3, 2009, the maximum guaranteed residual value at lease expiration was $0.6 million. Historically, payments related to these guarantees have been insignificant. We believe the likelihood of funding the guarantee obligation under any provision of the operating lease is remote and thus, we have not recognized a liability.

Pre-opening Costs

Costs associated with the start up and promotion of new store openings are expensed as incurred.

Advertising Costs

We incur advertising costs associated with print and broadcast advertisements. Advertising costs are charged to expense when the ad first runs. Advertising expense was $92.0 million, $109.9 million and $105.3 million, in 2008, 2007 and 2006, respectively. Advertising costs deferred and included in prepaid expenses in our consolidated balance sheets were $0.7 million and $1.3 million as of January 3, 2009, and December 29, 2007, respectively.

Insurance

We are self-insured for certain losses related to health and workers' compensation claims, although we do obtain third-party insurance coverage to limit exposure to these claims. We estimate our self-insured liabilities using a number of factors including historical claims experience and analysis of incurred but not reported claims. Our self-insurance liability was $4.8 million at January 3, 2009 and December 29, 2007, and is included in other current liabilities in our consolidated balance sheets.

Stock-Based Compensation

We record stock-based compensation expense based on the provisions of SFAS No. 123R, "*Share-Based Payment*" based on the award's fair value at the date of grant and the awards that are expected to vest. We recognize stock-based compensation expense over the period during which an employee is required to provide services in exchange for the award, or to their eligible retirement date, if earlier. We use the Black-Scholes-Merton option-pricing model to estimate the fair value of stock options and resulting compensation expense. The most significant inputs into the Black-Scholes-Merton option-pricing model are exercise price, our estimate of expected stock price volatility and the weighted-average expected life of the options. We include as part of cash flows from financing activities the benefit of tax deductions in excess of recognized compensation expense as prescribed in SFAS No. 123R. We adopted SFAS No. 123R at the beginning of 2006 using the modified prospective transition method.

See Note 6, *Shareholders' Equity*, for additional information on stock-based compensation.

Income Taxes

We recognize deferred tax assets and liabilities for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is established for any portion of deferred tax assets that are not considered more likely than not to be realized. We evaluate all available positive and negative

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Notes to Consolidated Financial Statements – (continued)

evidence, including the existence of cumulative year losses and our forecast of future taxable income, to assess the need for a valuation allowance on our deferred tax assets.

We recognize the benefits of tax positions based on the provisions of FASB Interpretation ("FIN") No. 48, "*Accounting for Uncertainty in Income Taxes.*" FIN No. 48 and related interpretations define when benefits of tax positions in the financial statements are recognized and provides guidance on the derecognition, measurement and classification of income tax uncertainties, along with any related interest and penalties. We adopted FIN No. 48 effective December 31, 2006. The adoption of FIN No. 48 and related interpretations did not materially affect our consolidated financial statements and, as a result, we did not record any cumulative effect adjustment upon adoption.

We classify interest and penalties on tax uncertainties as a component of income tax expense in our consolidated statements of operations.

(Loss) Income Per Share

Basic (loss) income per share excludes dilution and is computed by dividing net (loss) income attributable to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted (loss) income per share includes potentially dilutive common shares consisting of stock options, restricted stock and warrants using the treasury stock method. In 2008, we excluded shares of restricted stock and stock options from our computation of diluted net loss per share, as their inclusion would have had an anti-dilutive effect (i.e., resulted in lower loss per share).

Sources of Supply

We currently obtain materials and components used to produce our beds from outside sources. As a result, we are dependent upon suppliers that in some instances, are our sole source of supply. We are continuing our efforts to dual-source key components. The failure of one or more of our suppliers to provide us with materials or components on a timely basis could significantly impact our consolidated results of operations and net (loss) income per share. We believe we can obtain these raw materials and components from other sources of supply in the ordinary course of business, if necessary.

New Accounting Pronouncements

In February 2008, the FASB issued Financial Staff Position (FSP) No. 157-2, *Effective Date of FASB Statement No. 157*, which delays the effective date of SFAS No. 157 ("FSP 157-2") for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). SFAS No. 157 establishes a framework for measuring fair value and expands disclosures about fair value measurements. FSP 157-2 partially defers the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of this FSP. The adoption of SFAS No. 157 for all nonfinancial assets and nonfinancial liabilities is effective for us beginning January 4, 2009. We do not expect the adoption of FSP 157-2 to have a material impact on our consolidated financial statements.

In April 2008, the FASB issued FSP No. 142-3, *Determination of the Useful Life of Intangible Assets* ("FSP 142-3"). FSP 142-3 amends the factors to be considered in developing renewal or extension assumptions used to determine the useful life of intangible assets under SFAS No. 142, "Goodwill and Other Intangible Assets." Its intent is to improve the consistency between the useful life of an intangible asset and the period of expected cash flows used to measure its fair value. This FSP is effective prospectively for intangible assets acquired or renewed after January 1, 2009. We do not expect FSP 142-3 to have a material impact on our consolidated financial statements.

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(2) Inventories

Inventories consist of the following (in thousands):

	January 3, 2009	December 29, 2007
Raw materials	$ 4,280	$ 10,685
Work in progress	99	225
Finished goods	14,296	21,607
	$ 18,675	$ 32,517

Our finished goods inventory, as of January 3, 2009, was comprised of $5.6 million of finished beds, including retail display beds and deliveries in-transit to those customers who have utilized home delivery services, $2.7 million of finished components that were ready for assembly for the completion of beds, and $6.0 million of retail accessories.

Our finished goods inventory, as of December 29, 2007, was comprised of $5.9 million of finished beds, including retail display beds and deliveries in-transit to those customers who have utilized home delivery services, $10.0 million of finished components that were ready for assembly for the completion of beds, and $5.7 million of retail accessories.

(3) Property and Equipment

Property and equipment consist of the following (in thousands):

	January 3, 2009	December 29, 2007
Land	$ 1,999	$ 1,999
Leasehold improvements	90,720	94,451
Office furniture and equipment	3,997	5,109
Production machinery, computer equipment and software	68,130	81,770
Property under capital lease	1,163	—
Less: Accumulated depreciation and amortization	(112,735)	(102,920)
	$ 53,274	$ 80,409

During 2008, 2007 and 2006, we recorded asset impairment charges of $34.6 million, $0.4 million and $6.0 million, respectively. During the fourth quarter of fiscal 2008, we elected to abandon our plan to implement an integrated suite of SAP®-based applications in 2009 and recognized asset impairment charges totaling $27.6 million. In addition, during 2008 and 2007, we reviewed all of our stores for impairment and determined that certain store assets at underperforming stores were impaired. We recognized impairment charges of $7.0 million and $0.4 million, respectively, for the difference between the fair value and the carrying amounts of the related long-lived assets.

Our 2006 asset impairment charges were comprised of $5.4 million resulting from the abandonment of software we had been developing and $0.6 million resulting from the difference between the fair value and carrying amount of the related long-lived assets.

Asset impairment charges is one of our critical accounting estimates and requires management to make estimates about future events including sales growth rates, cash flows and asset fair values. We estimate fair values based on probability-weighted discounted cash flows, quoted market prices or other valuation techniques. Our 2008 quarterly store asset impairment charges reflected the deterioration of consumer spending and the more difficult economic environment as the year progressed. Our impairment calculations assume the ongoing availability of consumer credit and our ability to provide cost-effective consumer credit options. However, the recent tightening of credit standards, for our customers who seek extended financing from our third party financiers, was considered in our estimates. Predicting future events is inherently an imprecise activity. If actual results are not consistent with the estimates and assumptions used in our asset impairment calculations, we may incur additional impairment charges in the near term.

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Notes to Consolidated Financial Statements – (continued)

(4) Leases

Operating Leases

Rent expense was as follows (in thousands):

	2008	2007	2006
Facility Rents:			
Minimum rents	$ 38,157	$ 32,663	$ 27,579
Contingent rents	1,962	7,564	9,443
Total	$ 40,119	$ 40,227	$ 37,022
Equipment rents	$ 3,412	$ 2,753	$ 2,484

Capital Leases

During 2008, we entered into capital leases totaling $1.0 million, respectively, for certain computer and manufacturing equipment. At January 3, 2009, $0.3 million was included in other current liabilities and $0.5 million was included in other long-term liabilities in our consolidated balance sheet.

The aggregate minimum rental commitments under operating leases and future maturities of capital leases for subsequent years are as follows (in thousands):

	Operating	Capital
2009	$ 34,540	$ 302
2010	32,216	320
2011	26,715	223
2012	21,982	—
2013	17,419	—
Thereafter	25,017	—
	$ 157,889	$ 845

(5) Debt

Credit Agreement

In June 2006, we entered into a Credit Agreement (the “Credit Agreement”) with a syndicate of banks (the “Lenders”). The Credit Agreement, as amended to date, provides a revolving credit facility in an aggregate amount of $90 million to be used for general corporate purposes, which amount decreases to $85 million as of March 31, 2009 and to $80 million as of July 1, 2009. The Credit Agreement terminates in June 2010.

The Credit Agreement was amended on February 1, 2008 and on May 30, 2008 to allow greater flexibility under the existing financial covenants, provide additional financial covenants and monthly measurement of financial covenants, modify the credit limit and maturity date, increase the cost of borrowing, provide the Lenders with a collateral security interest in substantially all of our assets and those of our subsidiaries, and impose additional restrictions and covenants with respect to our operations.

We had outstanding borrowings of $79.2 million and $37.9 million, under the credit facility as of January 3, 2009, and December 29, 2007, respectively. We also had outstanding letters of credit of $5.9 million and zero as of January 3, 2009, and December 29, 2007, respectively. Outstanding letters of credit reduce the amounts available under the credit facility. At January 3, 2009, and December 29, 2007, $5.0 million and $62.1 million, respectively, were available under this credit facility. In early March 2009, we received a federal income tax refund of approximately $23.0 million. Pursuant to the terms of the Credit Agreement, these funds have been placed in a cash collateral account with the Lenders. We are in discussions with the Lenders regarding the potential use or application of these funds to address our near-term liquidity needs.

At January 3, 2009, borrowings under the credit facility bore interest at a floating rate and could be maintained as base rate loans (tied to the prime rate, plus a margin of up to 4.00% or the federal funds rate plus 5.00%) or as Eurocurrency rate loans (tied to LIBOR, plus a margin up to 5.0% depending on our leverage ratio, as defined). We also pay certain facility and agent fees. As of January 3, 2009, and December 29, 2007, interest rates on borrowings outstanding under the Credit Agreement were 6.0% and 5.2%, respectively. We are subject to certain financial covenants under the agreement, including a maximum leverage ratio, a minimum interest coverage ratio, minimum EBITDA requirements, and capital expenditure limits.

Pursuant to a series of amendments of the Credit Agreement, the Lenders have deferred to March 31, 2009 a reduction in the amount available under our line of credit from $90 million to $85 million that was previously scheduled to become effective as of December 1, 2008. Also pursuant to these amendments, the Lenders have waived compliance, through the close of business on March 30, 2009, with: (a) the minimum interest coverage ratio covenant of the Credit Agreement for the fiscal periods ending on or about December 31, 2008, January 31, 2009 and February 28, 2009, and (b) the minimum EBITDA covenant of the Credit Agreement for the fiscal period ending on or about December 31, 2008. Upon expiration of our most recent amendment on March 31, 2009, we will not be in compliance with certain financial covenants under the Credit Agreement. If we are unable to continue to obtain amendments from the Lenders that waive compliance with these financial covenants, our bank syndicate could place us in default under the terms of the Credit Agreement. A default under the Credit Agreement would enable the Lenders to seek immediate payment, severely constraining our operating flexibility and our ability to fund our business. Any further amendment of the Credit Agreement may significantly increase the cost of credit provided under the credit facility and related expenses, which may adversely impact our profitability.

In light of these increased uncertainties, we are considering options to enhance our financial flexibility and fund our operations, including the need to raise equity or debt capital. The issuance of any additional debt securities could materially and adversely impact our profitability and financial condition. The issuance of additional equity securities could be substantially dilutive to our existing shareholders.

At January 3, 2009, we had $1.1 million in deferred financing fees related to the Credit Agreement. If the Lenders have the right to demand payment before the Credit Agreement terminates, we would expense any remaining unamortized deferred financing fees.

(6) Shareholders' Equity

Stock-Based Compensation Plans

We compensate officers, directors and key employees with stock-based compensation under three stock plans approved by our shareholders in 1990, 1997 and 2004 and administered under the supervision of our Board of Directors ("Board"). At January 3, 2009, a total of 1,435,000 shares were available for future grant under the 2004 stock plan. Stock option awards are granted at exercise prices equal to the closing price of our stock on the date of grant. Generally, options vest proportionally over periods of three to four years from the dates of the grant and expire after ten years. Compensation expense is recognized ratably over the vesting period.

Stock Options

A summary of our stock option activity for the year ended January 3, 2009, is as follows (in thousands, except per share amounts):

	Stock Options	Weighted-Average Exercise Price per Share	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value [1]
Outstanding at December 29, 2007	5,274	$ 12.40	5.6	$ 7,749
Granted	797	3.43		
Exercised	(62)	1.50		
Canceled/Forfeited	(935)	14.93		
Outstanding at January 3, 2009	5,074	$ 10.67	4.9	$ —
Exercisable at January 3, 2009	3,537	$ 9.20	3.6	$ —

(1) Aggregate intrinsic value includes only those options where the exercise price is equal to or greater than the share price on the date of grant. As of

January 3, 2009, the intrinsic value of all outstanding stock options was zero.

Other information pertaining to options for the years ended January 3, 2009; December 29, 2007; and December 30, 2006 is as follows (in thousands, except per share amounts):

	2008	2007	2006
Weighted-average grant date fair value of stock options granted	$ 1.65	$ 8.94	$ 12.69
Total intrinsic value (at exercise) of stock options exercised	$ 115	$ 6,637	$ 28,507
Cash received from the exercise of stock options	$ 92	$ 3,489	$ 8,809
Stock-based compensation expense recognized in the consolidated statements of operations	$ 2,916	$ 4,528	$ 6,612
Excess income tax benefits from exercise of stock options	$ 19	$ 1,497	$ 8,565

At January 3, 2009, there was $6.4 million of total stock option compensation expense related to non-vested awards not yet recognized, which is expected to be recognized over a weighted-average period of 4.9 years.

Determining Fair Value

We estimated the fair value of stock options granted using the Black-Scholes-Merton option-pricing model and a single option award approach. Forfeitures are estimated using historical experience and projected employee turnover. A description of significant assumptions used to estimate the expected volatility, risk-free interest rate and expected term was as follows:

Expected Volatility – Expected volatility was determined based on implied volatility of our traded options and historical volatility of our stock price.

Risk-Free Interest Rate – The risk-free interest rate was based on the implied yield currently available on U.S. Treasury zero-coupon issues with a term equal to the expected term.

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Expected Term – Expected term represents the period that our stock-based awards are expected to be outstanding and was determined based on historical experience and anticipated future exercise patterns, giving consideration to the contractual terms of unexercised stock-based awards.

The assumptions used to calculate the fair value of awards granted during 2008, 2007 and 2006 using the Black-Scholes-Merton option-pricing model were as follows:

Valuation Assumptions	2008	2007	2006
Expected dividend yield	0%	0%	0%
Expected volatility	52%	50%	50%
Risk-free interest rate	2.5%	4.7%	4.7%
Expected term (in years)	5.3	5.2	5.6

Restricted and Performance Stock

We issue restricted and performance stock awards to certain employees in conjunction with our share-based compensation plan. The awards generally cliff-vest from three to five years based on continued employment ("time based"). Compensation expense related to time-based stock awards is determined on the grant-date based on the publicly quoted fair market value of our common stock and is charged to earnings on a straight-line basis over the vesting period. Performance stock may be earned and become vested in a specific percentage depending upon the extent to which the target performance is met as of the last day of the performance cycle ("performance based"). Total compensation expense related to time-based restricted and performance-based stock awards was $0.8 million, $1.7 million and $1.7 million, for the years ended January 3, 2009; December 29, 2007; and December 30, 2006, respectively. There were 38,000 restricted and performance stock awards vested at January 3, 2009. All outstanding restricted and performance stock awards were unvested at December 29, 2007, and December 30, 2006. Restricted and performance stock activity was as follows for the year ended January 3, 2009 (in thousands, except per share amounts):

	Restricted Stock	Weighted-Average Grant Date Fair Value	Performance Stock	Weighted-Average Grant Date Fair Value
Outstanding at December 29, 2007	428	$ 15.84	152	$ 21.44
Granted	137	4.05	173	3.73
Canceled/Forfeited	(205)	12.63	(74)	10.26
Outstanding at January 3, 2009	360	$ 13.20	251	$ 12.36

At January 3, 2009, there was $2.5 million of unrecognized compensation expense related to non-vested restricted and performance share awards, which is expected to be recognized over a weighted-average period of 2.0 years.

Repurchases of Common Stock

On April 20, 2007, our Board authorized the repurchase of up to an additional $250.0 million of our common stock, bringing the total availability under our share repurchase program to $290.0 million. During 2008, we did not repurchase any shares of common stock. During 2007, we repurchased and retired 7,617,000 shares through open market purchases at a cost of $131.9 million (based on trade dates), respectively. During 2006, we repurchased and retired 3,889,000 shares through open market purchases at a cost of $79.7 million (based on trade dates). As of January 3, 2009, the remaining authorization under our share repurchase program was $206.8 million. There is no expiration date governing the period over which we can repurchase shares. We currently have no plans to repurchase our stock under this authorization.

**SELECT COMFORT CORPORATION
AND SUBSIDIARIES**

Notes to Consolidated Financial Statements – (continued)

The cost of stock repurchases is first charged to additional paid-in capital. Once additional paid-in capital is reduced to zero, any additional amounts are charged to (accumulated deficit) retained earnings.

Net (Loss) Income per Common Share

The following computations reconcile net (loss) income per share – basic with net (loss) income per share – diluted (in thousands, except per share amounts):

	2008	2007	2006
Net (loss) income	$ (70,177)	$ 27,620	$ 47,183
Reconciliation of weighted-average shares outstanding:			
Basic weighted-average shares outstanding	44,186	46,536	52,837
Effect of dilutive securities:			
Options	—	1,455	2,529
Warrants	—	—	28
Restricted shares	—	301	193
Diluted weighted-average shares outstanding	44,186	48,292	55,587
Net (loss) income per share – basic	$ (1.59)	$ 0.59	$ 0.89
Net (loss) income per share – diluted	(1.59)	0.57	0.85

Additional potentially dilutive stock options totaling 5,124,000, 2,441,000 and 1,077,000 for the years 2008, 2007 and 2006, respectively, have been excluded from diluted EPS because these securities' exercise prices were greater than the average market price of our common shares. In addition, we excluded 444,000 shares of restricted stock and 212,000 stock options from our computation of diluted net loss per share for 2008, as their inclusion would have had an anti-dilutive effect (i.e., resulted in a lower loss per share).

(7) Other (Expense) Income, Net

Other (expense) income, net, consisted of the following (in thousands):

	2008	2007	2006
Interest income	$ 90	$ 1,079	$ 3,018
Interest expense	(4,434)	(1,163)	—
Write-off unamortized debt cost	(131)	—	—
Capitalized interest expense	1,190	314	—
Realized loss on sales of marketable debt securities	—	(270)	—
Other (expense) income, net	$ (3,285)	$ (40)	$ 3,018

**SELECT COMFORT CORPORATION
AND SUBSIDIARIES**

Notes to Consolidated Financial Statements – (continued)

(8) Income Taxes

The (benefit) expense for income taxes consisted of the following (in thousands):

	2008	2007	2006
Current:			
Federal	$ (26,910)	$ 19,454	$ 30,572
State	(732)	3,672	5,738
	(27,642)	23,126	36,310
Deferred:			

Federal	26,853	(6,348)	(6,387)
State	(1,777)	(932)	(1,278)
	25,076	(7,280)	(7,665)
Income tax (benefit) expense	$ (2,566)	$ 15,846	$ 28,645

Effective tax rates differ from statutory federal income tax rates as follows:

	2008	2007	2006
Statutory federal income tax rate	(35.0%)	35.0%	35.0%
Valuation allowance	36.9	—	—
State income taxes, net of federal benefit	(4.5)	4.1	3.8
Other	(0.9)	(2.6)	(1.0)
	(3.5%)	36.5%	37.8%

We file income tax returns with the U.S. federal government and various state jurisdictions. In the normal course of business, we are subject to examination by federal and state taxing authorities. We are no longer subject to federal or state income tax examinations for years prior to 2004.

Deferred Income Taxes

The tax effects of temporary differences that give rise to deferred income taxes were as follows (in thousands):

	2008	2007
Deferred tax assets:		
Current:		
Compensation and benefits	$ 2,689	$ 3,399
Warranty and returns liabilities	1,935	2,332
Deferred rent and lease incentives	984	471
Other	609	614
Long-term:		
Property and equipment	12,161	13,502
Stock-based compensation	6,835	5,443
Deferred rent and lease incentives	3,324	3,261
Warranty liability	2,008	2,824
Net operating loss, capital loss and tax credit carryforwards	2,933	101
Other	719	487
Total gross deferred tax assets	34,197	32,434
Valuation allowance	(26,933)	(94)
Total net deferred tax assets	$ 7,264	$ 32,340

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At January 3, 2009, we had net operating loss carryforwards for state income tax purposes of $71.1 million which will expire between 2011 and 2028.

In accordance with SFAS No. 109, "Accounting for Income Taxes," we evaluate our deferred income taxes quarterly to determine if valuation allowances are required. SFAS No. 109 requires that companies assess whether valuation allowances should be established for any deferred tax assets that are not considered more likely than not to be realized, using all available evidence, both positive and negative. This assessment considers, among other matters, the nature, frequency, and severity of recent losses, forecasts of future profitability, taxable income in available carryback periods and tax planning strategies. In making such judgments, significant weight is given to evidence that can be objectively verified.

We had a $26.9 million and $94,000 tax valuation allowance at January 3, 2009, and December 29, 2007, respectively. Due to our net loss in 2008, our expectations that macro-economic trends and consumer confidence will remain weak throughout 2009, and uncertainty regarding future taxable income; we determined that it was more likely than not that a portion of our deferred tax assets would not be realized. In the fourth quarter of 2008, we established a $26.8 million valuation allowance against deferred tax assets that could not be realized through taxable income earned in available carryback periods. If and when our operating performance improves on a sustained basis, our conclusion regarding the need for the $26.8 million deferred tax valuation allowance could change, resulting in the reversal of some or all of the valuation allowance in future periods. We also have a $94,000 valuation allowance at January 3, 2009, and December 29, 2007, related to a capital loss carryforward that will expire in 2012 if not utilized.

Unrecognized Tax Benefits

At January 3, 2009, and December 29, 2007, the total amounts of unrecognized tax benefits for uncertain tax positions were $155,000 and $97,000, respectively, that if recognized, would impact the effective tax rate. The amount of unrecognized tax benefits are not expected to change materially within the next 12 months.

A reconciliation of the beginning and ending amounts of unrecognized tax benefits for 2007 and 2008 was as follows (in thousands):

	Federal And	Accrued Interest	Gross Unrecognized

	State Tax	And Penalties	Income Tax Benefits
Balance December 31, 2006	$ 228	$ 24	$ 252
Increases related to prior-year tax positions	—	8	8
Decreases related to prior-year tax positions	(24)	—	(24)
Lapse of statute of limitations	(107)	(32)	(139)
Balance December 29, 2007	$ 97	$ —	$ 97
Decreases related to prior-year tax positions	(50)	—	(50)
Increases related to prior-year tax positions	105	3	108
Balance January 3, 2009	$ 152	$ 3	$ 155

In 2008, 2007 and 2006, we included $3,000, $8,000 and $10,000, respectively, of penalties and interest in income tax (benefit) expense.

(9) Employee Benefit Plans

Profit Sharing and 401(k) Plan

Under our profit sharing and 401(k) plan, eligible employees may defer up to 50% of their compensation on a pre-tax basis, subject to Internal Revenue Service limitations. Each year, we may make a discretionary contribution equal to a percentage of the employee's contribution. Beginning in the fourth quarter of fiscal 2008, due to the challenging business environment, we

discontinued our discretionary 401(k) contribution. During 2008, 2007 and 2006, our contributions, net of forfeitures, were $1.9 million, $2.8 million and $2.5 million, respectively.

Employee Stock Purchase Plan

We had an employee stock purchase plan ("ESPP") which permitted employees to purchase our common stock at a 5% discount based on the average price of the stock on the last business day of the offering period (calendar quarter basis). Purchases were funded by employee payroll deductions during the offering period. Employees purchased 236,847 shares in 2008, 68,670 shares in 2007 and 60,464 shares in 2006 under this plan. At January 3, 2009, and December 29, 2007, ESPP participants had accumulated $132,000 and $192,000, respectively, to purchase our common stock. We discontinued our ESPP plan at the beginning of 2009.

(10) Commitments and Contingencies

On April 25, 2008, a lawsuit was filed against one of our subsidiaries in Superior Court in Santa Clara County, California by one of our customers. The complaint asserted various claims related to products liability, breach of warranty, concealment, intentional misrepresentation and negligent misrepresentation and sought class certification. The complaint alleged that products sold by us prior to 2006 had a unique propensity to develop mold, alleged that the plaintiff suffered adverse health effects, and sought various forms of legal and equitable relief, including without limitation unspecified damages, punitive and exemplary damages, attorneys' fees and costs, and injunctive relief. We removed the case to the U.S. District Court for the Northern District of California. On September 30, 2008, the Court granted our motion to dismiss and strike the purported class action claims, and allowed the plaintiff leave to amend the complaint. On October 30, 2008, the plaintiff filed an amended complaint alleging facts similar to those asserted in the initial complaint and asserting additional claims, including antitrust and RICO claims. We have filed a motion to dismiss the amended complaint on the same basis that the Court dismissed the original complaint, and our motion remains pending before the Court. As of January 3, 2009, no accrual had been established as we believe that the complaint is without merit and we intend to vigorously defend the claims.

We are involved from time to time in various other legal proceedings arising in the ordinary course of our business, including primarily commercial, employment and intellectual property claims. In accordance with generally accepted accounting principles in the United States, we record a liability in our consolidated financial statements with respect to any of these matters when it is both probable that a liability has been incurred and the amount of the liability can be reasonably estimated. With respect to these other matters, we believe that we have valid defenses to claims asserted against us and we do not expect the outcome of these other matters to have a material effect on our consolidated results of operations or financial position. Litigation, however, is inherently unpredictable, and it is possible that the ultimate outcome of one or more claims asserted against us could adversely impact our results of operations or financial position. We expense legal costs as incurred.

Consumer Credit Arrangements

We refer customers seeking extended financing to certain third party financiers ("Card Servicers"). The Card Servicers, if credit is granted, establish the interest rates, fees, and all other terms and conditions of the customer's account based on their evaluation of the creditworthiness of the customers. As the receivables are owned by the Card Servicers, at no time are the receivables purchased or acquired from us. We are not liable to Card Servicers for our customers' credit defaults. In connection with customer purchases financed under these arrangements, the Card Servicers pay us an amount equal to the total amount of such purchases, net of promotional related discounts. The amounts financed and uncollected from Card Servicers under the program were included in accounts receivable and totaled $1.0 million and $2.3 million as of January 3, 2009, and December 29, 2007, respectively.

Termination of our agreements with Card Servicers, any material change to the terms of agreements with Card Servicers or in the availability or terms of credit for our customers from Card Servicers, or any delay in securing replacement credit sources, could materially affect our consolidated results of operations or financial position.

Our agreement under which GE Money Bank offers to our qualified customers revolving credit arrangements to finance purchases from us (the "GE Agreement") contains certain financial covenants, including maximum leverage ratio and minimum interest coverage. As our recent results placed us outside of these financial covenants, we were required under the terms of the GE Agreement to provide GE Money Bank with a $2.7 million letter of credit as collateral security.

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Commitments

As of January 3, 2009, we had $159.2 million of inventory purchase commitments with our suppliers as part of the normal course of business. There are a limited number of supply contracts that contain penalty provisions for failure to purchase contracted quantities. We do not expect potential payments under these provisions to materially affect our consolidated results of operations or financial position.

(11) Summary of Quarterly Financial Data (unaudited)

The following is a condensed summary of actual quarterly results for 2008 and 2007 (in thousands, except per share amounts):

2008	Fourth	Third	Second	First
Net sales	$ 131,073	$ 157,231	$ 152,055	$ 168,165
Gross profit	73,246	97,756	90,644	96,926
Operating (loss) income	(50,217)	2,052	(10,251)	(11,042)
Net (loss) income	(57,436)	983	(6,591)	(7,133)
Net (loss) income per share – diluted	(1.30)	0.02	(0.15)	(0.16)

2007	Fourth	Third	Second	First
Net sales	$ 190,672	$ 213,070	$ 178,991	$ 216,509
Gross profit	111,542	131,178	109,527	134,168
Operating income	2,799	19,077	4,803	16,827
Net income	2,168	11,863	2,912	10,677
Net income per share – diluted	0.05	0.26	0.06	0.21

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ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Conclusions Regarding the Effectiveness of Disclosure Controls and Procedures

We maintain disclosure controls and procedures, as defined in Exchange Act Rule 13a-15(e), that are designed to ensure that information required to be disclosed by the company in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the company's management, including its principal executive officer and principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this annual report. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this annual report.

Management's Report on Internal Control Over Financial Reporting

Select Comfort's management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Select Comfort's management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Management, with the participation of our principal executive officer and principal financial officer, evaluated the effectiveness of our internal control over financial reporting based on the framework in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation under these criteria, management concluded that our internal control over financial reporting was effective as of January 3, 2009.

Fourth Quarter Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the quarter ended January 3, 2009 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information under the captions "Election of Directors," "Corporate Governance" and "Section 16(a) Beneficial Ownership Reporting Compliance" in our Proxy Statement for our 2009 Annual Meeting of Shareholders is incorporated herein by reference. Information concerning our executive officers is included in Part I of this report under the caption "Executive Officers of the Registrant."

We have adopted a Code of Business Conduct applicable to our directors, officers and employees (including our principal executive officer, principal financial officer, principal accounting officer and controller). The Code of Business Conduct is available on the Investor Relations section of our Web site at *http://www.selectcomfort.com*. In the event that we amend or waive any of the provisions of the Code of Business Conduct applicable to our principal executive officer, principal financial officer, principal accounting officer and controller, we intend to disclose the same on our Web site at *http://www.selectcomfort.com*.

ITEM 11. EXECUTIVE COMPENSATION

The information under the caption "Executive Compensation" in our Proxy Statement for our 2009 Annual Meeting of Shareholders is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information under the caption "Equity Compensation Plan Information" in Item 5 of this Annual Report on Form 10-K and the information under the caption "Stock Ownership of Management and Certain Beneficial Owners" in our Proxy Statement for our 2009 Annual Meeting of Shareholders is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information under the caption "Corporate Governance" in our Proxy Statement for our 2009 Annual Meeting of Shareholders is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information under the caption "Approval of Selection of Independent Registered Public Accounting Firm" in our Proxy Statement for our 2009 Annual Meeting of Shareholders is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) **Consolidated Financial Statements and Schedule**

(1) Consolidated Balance Sheets

Consolidated Statements of Operations

Consolidated Statements of Shareholders' Equity

Consolidated Statements of Cash Flows

Notes to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm on Internal Control over Financial Reporting

Report of Independent Registered Public Accounting Firm on Consolidated Financial Statements and Financial Statement Schedule

(2) **Consolidated Financial Statement Schedule**

The following Report and financial statement schedule are included in this Part IV.

Schedule II – Valuation and Qualifying Accounts

All other schedules are omitted because they are not applicable or the required information is included in the consolidated financial statements or notes thereto.

(3) **Exhibits**

The exhibits to this Report are listed in the Exhibit Index below.

We will furnish a copy of any of the exhibits referred to above at a reasonable cost to any shareholder upon receipt of a written request. Requests should be sent to: Select Comfort Corporation, Investor Relations Department, 9800 59th Avenue North, Minneapolis, Minnesota 55442.

The following is a list of each management contract or compensatory plan or arrangement required to be filed as an exhibit to this Annual Report on Form 10-K pursuant to Item 15(c):

1. Select Comfort Corporation 1990 Omnibus Stock Option Plan, as amended and restated
2. Select Comfort Corporation 1997 Stock Incentive Plan, as amended and restated
3. Form of Incentive Stock Option Agreement under the 1990 and 1997 Stock Plans
4. Form of Performance Based Stock Option Agreement under the 1990 and 1997 Stock Plans
5. Select Comfort Corporation 2004 Stock Incentive Plan (Amended and Restated as of January 1, 2007)
6. Form of Nonstatutory Stock Option Award Agreement under the 2004 Stock Incentive Plan
7. Form of Restricted Stock Award Agreement under the 2004 Stock Incentive Plan
8. Form of Performance Stock Award Agreement under the 2004 Stock Incentive Plan
9. Form of Nonstatutory Stock Option Award Agreement (Subject to Performance Adjustment) under the 2004 Stock Incentive Plan
10. Select Comfort Profit Sharing and 401(K) Plan – 2007 Restatement
11. Select Comfort Executive Investment Plan, as Amended and Restated October 29, 2008

12. Select Comfort Executive and Key Employee Incentive Plan
13. Employment Letter from the Company to William R. McLaughlin dated March 3, 2000
14. Employment Letter from the Company to William R. McLaughlin dated March 2, 2006
15. Letter Agreement between William R. McLaughlin and Select Comfort Corporation dated as of February 21, 2008
16. Amended and Restated Non-Statutory Stock Option Agreement between Select Comfort Corporation and William R. McLaughlin dated as of April 22, 2008
17. Separation Agreement between the Company and Catherine B. Hall dated October 22, 2008
18. Employment Letter from the Company to Kathryn V. Roedel dated March 8, 2005
19. Employment Letter from the Company to Wendy L. Schoppert dated March 15, 2005
20. Employment Letter from the Company to Mark A. Kimball dated April 22, 1999
21. Summary of Executive Health Program
22. Summary of Executive Tax and Financial Planning Program
23. Amended and Restated Select Comfort Corporation Executive Severance Pay Plan
24. First Amendment to Amended and Restated Select Comfort Corporation Executive Severance Pay Plan
25. Summary of Non-Employee Director Compensation
26. Amended and Restated Select Comfort Corporation Non-Employee Director Equity Plan

SIGNATURES

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

SELECT COMFORT CORPORATION
(Registrant)

Dated: March 19, 2009

By: /s/ William R. McLaughlin
William R. McLaughlin
Chief Executive Officer
(principal executive officer)

By: /s/ James C. Raabe
James C. Raabe
Chief Financial Officer
(principal financial and accounting officer)

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POWER OF ATTORNEY

Know all persons by these presents, that each person whose signature appears below constitutes and appoints William R. McLaughlin, James C. Raabe and Mark A. Kimball, and each of them, as such person's true and lawful attorneys-in-fact and agents, with full power of substitution and resubstitution, for such person and in such person's name, place and stead, in any and all capacities, to sign any and all amendments to this Report, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as such person might or could do in person, hereby ratifying and confirming that all said attorneys-in-fact and agents, or any of them or their or such person's substitute or substitutes, may lawfully do or cause to be done by virtue thereof.

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

NAME	TITLE	DATE
/s/ Ervin R. Shames Ervin R. Shames	Chairman of the Board	March 16, 2009
/s/ William R. McLaughlin William R. McLaughlin	Director	March 19, 2009
/s/ Thomas J. Albani Thomas J. Albani	Director	March 13, 2009
/s/ Christine M. Day Christine M. Day	Director	March 19, 2009
/s/ Stephen L. Gulis, Jr. Stephen L. Gulis, Jr.	Director	March 13, 2009
/s/ Christopher P. Kirchen Christopher P. Kirchen	Director	March 10, 2009
/s/ David T. Kollat David T. Kollat	Director	March 12, 2009
/s/ Brenda J. Lauderback Brenda J. Lauderback	Director	March 13, 2009
/s/ Michael A. Peel Michael A. Peel	Director	March 11, 2009
/s/ Jean-Michel Valette Jean-Michel Valette	Director	March 17, 2009

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SELECT COMFORT CORPORATION
EXHIBIT INDEX TO ANNUAL REPORT ON FORM 10-K
FOR THE YEAR ENDED JANUARY 3, 2009

Exhibit No.	Description	Method Of Filing
3.1	Third Restated Articles of Incorporation of the Company, as	Incorporated by reference to Exhibit 3.1 contained in Select

	amended	Comfort's Annual Report on Form 10-K for the fiscal year ended January 1, 2000 (File No. 0-25121)
3.2	Articles of Amendment to Third Restated Articles of Incorporation of the Company	Incorporated by reference to Exhibit 3.1 contained in Select Comfort's Current Report on Form 8-K filed May 16, 2006 (File No. 0-25121)
3.3	Restated Bylaws of the Company	Incorporated by reference to Exhibit 3.1 contained in Select Comfort's Current Report on Form 8-K filed May 21, 2007 (File No. 0-25121)
10.1	Net Lease Agreement dated December 3, 1993 between the Company and Opus Corporation	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Registration Statement on Form S-1, as amended (Reg. No. 333-62793)
10.2	Amendment of Lease dated August 10, 1994 between the Company and Opus Corporation	Incorporated by reference to Exhibit 10.2 contained in the Select Comfort's Registration Statement on Form S-1, as amended (Reg. No. 333-62793)
10.3	Second Amendment to Lease dated May 10, 1995 between the Company and Rushmore Plaza Partners Limited Partnership (successor to Opus Corporation)	Incorporated by reference to Exhibit 10.3 contained in Select Comfort's Registration Statement on Form S-1, as amended (Reg. No. 333-62793)
10.4	Letter Agreement dated as of October 5, 1995 between the Company and Rushmore Plaza Partners Limited Partnership	Incorporated by reference to Exhibit 10.4 contained in Select Comfort's Registration Statement on Form S-1, as amended (Reg. No. 333-62793)
10.5	Third Amendment of Lease, Assignment and Assumption of Lease and Consent dated as of January 1, 1996 among the Company, Rushmore Plaza Partners Limited Partnership and Select Comfort Direct Corporation	Incorporated by reference to Exhibit 10.5 contained in Select Comfort's Registration Statement on Form S-1, as amended (Reg. No. 333-62793)
10.6	Fourth Amendment to Lease dated June 30, 2003 between Cabot Industrial Properties, L.P. (successor to Rushmore Plaza Partners Limited Partnership) and Select Comfort Direct Corporation	Incorporated by reference to Exhibit 10.6 contained in Select Comfort's Annual report on Form 10-K for the fiscal year ended January 3, 2004 (File No. 0-25121)
10.7	Fifth Amendment to Lease dated August 28, 2006 between Cabot Industrial Properties, L.P. (successor to Rushmore Plaza Partners Limited Partnership) and Select Comfort Direct Corporation	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Quarterly report on Form 10-Q for the quarter ended September 30, 2006 (File No. 0-25121)

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Exhibit No.	Description	Method Of Filing
10.8	Lease Agreement dated as of September 19, 2002 between the Company and Blind John, LLC (as successor to Frastacky (US) Properties Limited Partnership)	Incorporated by reference to Exhibit 10.6 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 28, 2002 (File No. 0-25121)
10.9	Lease Agreement dated September 30, 1998 between the Company and ProLogis Development Services Incorporated	Incorporated by reference to Exhibit 10.12 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 28, 2002 (File No. 0-25121)
10.10	Net Lease Agreement (Build-to-Suit) by and between Opus Northwest LLC, as Landlord, and Select Comfort Corporation, as Tenant, dated July 26, 2006	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Quarterly report on Form 10-Q for the quarter ended July 1, 2006 (File No. 0-25121)
10.11	Select Comfort Corporation 1990 Omnibus Stock Option Plan, as amended and restated	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Quarterly Report on Form 10-Q for the quarter ended October 2, 1999 (File No. 0-25121)
10.12	Select Comfort Corporation 1997 Stock Incentive Plan, as amended and restated	Incorporated by reference to Exhibit 10.8 contained in Select Comfort's Quarterly Report on Form 10-Q for the quarter ended June 30, 2001 (File No. 0-25121)
10.13	Form of Incentive Stock Option Agreement under the 1990 and 1997 Stock Plans	Incorporated by reference to Exhibit 10.16 contained in the Company's Registration Statement on Form S-1, as amended (Reg. No. 333-62793)
10.14	Form of Performance Based Stock Option Agreement under the 1990 and 1997 Stock Plans	Incorporated by reference to Exhibit 10.17 contained in Select Comfort's Registration Statement on Form S-1, as amended (Reg. No. 333-62793)
10.15	Select Comfort Corporation 2004 Stock Incentive Plan (Amended and Restated as of January 1, 2007)	Incorporated by reference to Exhibit 10.16 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 30, 2006 (File No. 0-25121)
10.16	Form of Nonstatutory Stock Option Award Agreement under the Select Comfort Corporation 2004 Stock Incentive Plan	Incorporated by reference to Exhibit 10.28 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended

December 31, 2005 (File No. 0-25121)

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Exhibit No.	Description	Method Of Filing
10.17	Form of Restricted Stock Award Agreement under the Select Comfort Corporation 2004 Stock Incentive Plan	Incorporated by reference to Exhibit 10.29 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 (File No. 0-25121)
10.18	Form of Performance Stock Award Agreement under the Select Comfort Corporation 2004 Stock Incentive Plan	Incorporated by reference to Exhibit 10.30 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 (File No. 0-25121)
10.19	Form of Nonstatutory Stock Option Award Agreement (Subject to Performance Adjustment) under the Select Comfort Corporation 2004 Stock Incentive Plan	Incorporated by reference to Exhibit 10.20 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 30, 2006 (File No. 0-25121)
10.20	Select Comfort Profit Sharing and 401(K) Plan – 2007 Restatement	Incorporated by reference to Exhibit 10.22 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 30, 2006 (File No. 0-25121)
10.21	Select Comfort Executive Investment Plan, as Amended and Restated October 29, 2008	Filed herewith.
10.22	Select Comfort Executive and Key Employee Incentive Plan	Incorporated by reference to Exhibit 10.22 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 30, 2000 (File No. 0-25121)
10.23	Employment Letter from the Company to William R. McLaughlin dated March 3, 2000	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Quarterly Report on Form 10-Q for the quarter ended April 1, 2000 (File No. 0-25121)
10.24	Employment Letter from the Company to William R. McLaughlin dated March 2, 2006	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed March 6, 2006 (File No. 0-25121)
10.25	Letter Agreement between William R. McLaughlin and Select Comfort Corporation dated as of February 21, 2008	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed February 27, 2008 (File No. 0-25121)
10.26	Amended and Restated Non-Statutory Stock Option Agreement between Select Comfort Corporation and William R. McLaughlin dated as of April 22, 2008	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed April 24, 2008 (File No. 0-25121)
10.27	Separation Agreement between the Company and Catherine B. Hall dated October 22, 2008	Filed herewith.

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Exhibit No.	Description	Method Of Filing
10.28	Employment Letter from the Company to Kathryn V. Roedel dated March 8, 2005	Incorporated by reference to Exhibit 10.17 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 (File No. 0-25121)
10.29	Employment Letter from the Company to Wendy L. Schoppert dated March 15, 2005	Incorporated by reference to Exhibit 10.18 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 (File No. 0-25121)
10.30	Employment Letter from the Company to Mark A. Kimball dated April 22, 1999	Incorporated by reference to Exhibit 10.25 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended January 1, 2000 (File No. 0-25121)
10.31	Summary of Executive Health Program	Incorporated by reference to Exhibit 10.36 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 (File No. 0-25121)
10.32	Summary of Executive Tax and Financial Planning Program	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed January 3, 2005 (File No. 0-25121)
10.33	Amended and Restated Select Comfort Corporation Executive	Incorporated by reference to Exhibit 10.1 contained in Select

	Severance Pay Plan, dated as of August 21, 2008	Comfort's Current Report on Form 8-K filed August 21, 2008 (File No. 0-25121)
10.34	First Amendment to Amended and Restated Select Comfort Corporation Executive Severance Pay Plan	Filed herewith
10.35	Summary of Non-Employee Director Compensation	Incorporated by reference to Exhibit 10.32 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 (File No. 0-25121)
10.36	Amended and Restated Select Comfort Corporation Non-Employee Director Equity Plan	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed May 1, 2006 (File No. 0-25121)
10.37	Supply Agreement dated October 3, 2006 between the Company and Supplier (1)	Incorporated by reference to Exhibit 10.39 contained in Select Comfort's Annual Report on Form 10-K for the fiscal year ended December 30, 2006 (File No. 0-25121)

Exhibit No.	Description	Method Of Filing
10.38	Amended and Restated Private Label Consumer Credit Card Program Agreement dated as of December 14, 2005 between GE Money Bank and Select Comfort Corporation and Select Comfort Retail Corporation (1)	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed December 20, 2005 (File No. 0-25121)
10.39	First Amendment to Amended and Restated Private Label Consumer Credit Card Program Agreement dated as of April 23, 2007 between GE Money Bank and Select Comfort Corporation and Select Comfort Retail Corporation	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed April 27, 2007 (File No. 0-25121)
10.40	Second Amendment to Amended and Restated Private Label Consumer Credit Card Program Agreement dated as of February 1, 2008 between GE Money Bank and Select Comfort Corporation and Select Comfort Retail Corporation	Incorporated by reference to Exhibit 10.3 contained in Select Comfort's Current Report on Form 8-K filed February 7, 2008 (File No. 0-25121)
10.41	Amended and Restated Exclusive Supplier Agreement between Radisson Hotels International, Inc. and Select Comfort Corporation (1)	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Quarterly Report on Form 10-Q for the quarter ended June 30, 2007 (File No. 0-25121)
10.42	Credit Agreement dated as of June 9, 2006 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed June 14, 2006 (File No. 0-25121)
10.43	Amendment No. 1 to Credit Agreement dated as of June 28, 2007 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed February 7, 2008 (File No. 0-25121)
10.44	Amendment No. 2 to Credit Agreement dated as of February 1, 2008 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed February 7, 2008 (File No. 0-25121)

Exhibit No.	Description	Method Of Filing
10.45	Amendment No. 3 to Credit Agreement dated as of May 30, 2008 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed June 2, 2008 (File No. 0-25121)

	Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	
10.46	Amendment No. 4 to Credit Agreement dated as of December 2, 2008 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed December 8, 2008 (File No. 0-25121)
10.47	Amendment No. 5 to Credit Agreement dated as of January 2, 2009 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed January 8, 2009 (File No. 0-25121)
10.48	Amendment No. 6 to Credit Agreement dated as of January 15, 2009 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed January 22, 2009 (File No. 0-25121)
10.49	Amendment No. 7 to Credit Agreement dated as of January 31, 2009 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed February 5, 2009 (File No. 0-25121)
10.50	Amendment No. 8 to Credit Agreement dated as of February 28, 2009 among Select Comfort Corporation, the subsidiary borrowers from time to time party thereto, JPMorgan Chase Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent and JPMorgan Chase Bank, National Association, Bank of America, N.A., Citicorp USA, Inc., Wells Fargo Bank, National Association and Branch Banking and Trust Co., as Lenders	Incorporated by reference to Exhibit 10.1 contained in Select Comfort's Current Report on Form 8-K filed March 2, 2009 (File No. 0-25121)

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Exhibit No.	Description	Method Of Filing
21.1	Subsidiaries of the Company	Filed herewith
23.1	Consent of Independent Registered Public Accounting Firm	Filed herewith
24.1	Power of Attorney	Included on signature page
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith

(1) Confidential treatment has been granted by the Securities and Exchange Commission with respect to designated portions contained within document. Such portions have been omitted and filed separately with the Securities and Exchange Commission pursuant to Rule 24b-2 of the Securities and Exchange Act of 1934, as amended.

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SELECT COMFORT CORPORATION AND SUBSIDIARIES
Schedule II – Valuation and Qualifying Accounts
(in thousands)

Description	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions From Reserves	Balance at End of Period
Allowance for doubtful accounts				
2008	$ 876	$ 814	$ 977	713
2007	529	1,035	688	$ 876
2006	552	676	699	529
Accrued sales returns				
2008	$ 3,751	$ 34,410	$ 35,417	$ 2,744
2007	3,907	43,716	43,872	3,751
2006	5,403	42,508	44,004	3,907

Exhibit 10.21

SELECT COMFORT

EXECUTIVE INVESTMENT PLAN

(January 1, 2009 Revision)

As Amended and Restated on October 29, 2008

ADOPTION CERTIFICATE

WHEREAS, on December 20, 2002, Select Comfort Corporation adopted the Select Comfort Executive Investment Plan; and

WHEREAS, Select Comfort Corporation adopted the First Declaration of Amendment to the Select Comfort Executive Investment Plan effective April 1, 2003 ("First Amendment"); and

WHEREAS, Select Comfort Corporation adopted the Second Declaration of Amendment to the Select Comfort Executive Investment Plan effective December 20, 2002 ("Second Amendment"); and

WHEREAS, Select Comfort Corporation adopted the Third Declaration of Amendment to the Select Comfort Executive Investment Plan effective February 16, 2004 ("Third Amendment", and together with the First Amendment, Second Amendment, and Third Amendment, the "Prior Amendments").

NOW, THEREFORE, Select Comfort Corporation hereby adopts this Amended and Restated Select Comfort Executive Investment Plan (January 1, 2009 Revision) in the form attached hereto pursuant to the authority granted by Select Comfort Corporation's Board of Directors, to integrate the Prior Amendments, and reflect additional amendments.

SELECT COMFORT CORPORATION

Attest:	/s/ Mitchell W. Johnson	By	/s/ Mark A. Kimball
Title:	Vice President & Assistant Secretary	Its	Senior Vice President & General Counsel

October 29, 2008

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SELECT COMFORT
EXECUTIVE INVESTMENT PLAN

ARTICLE 1.
DESCRIPTION

1.1 Plan Name.

The name of the Plan is the "Select Comfort Executive Investment Plan."

1.2 Plan Purpose.

The purposes of the Plan are to:

(a) assist the Participating Employers in attracting and retaining Qualified Employees,

(b) provide a tax-deferred capital accumulation vehicle for Qualified Employees, and

(c) encourage additional retirement savings by Qualified Employees.

1.3 Plan Type.

The Plan is an unfunded plan maintained primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees. It is intended that the Plan is exempt from the provisions of Parts 2, 3 and 4 of Subtitle B of Title I of ERISA by operation of sections 201(2), 301(a)(3) and 401(a)(4) thereof, respectively, and from the provisions of Title IV of ERISA, to the extent otherwise applicable, by operation of section 4021(b)(6) thereof. The Plan is also intended to be unfunded for tax purposes. The Plan will be construed and administered in a manner that is consistent with and gives effect to the foregoing. All amounts defined under the Plan shall be subject to the provisions of Code section 409A. The Plan is intended to comply in form and operation with Code Section 409A.

1.4 Plan Effective Date.

The Plan is effective as of December 20, 2002. The plan as amended and restated is effective January 1, 2009 or such earlier date specified herein.

ARTICLE 2.
PARTICIPATION

2.1 Eligibility.

(a) First Day of Plan Year. Prior to the beginning of each Plan Year, the Administrator will determine which Qualified Employees, if any, are eligible to defer Base Salary pursuant to Sections 3.2(a), 3.3(a) and 3.4(a) and Bonus pursuant to Sections 3.2(b), 3.3(b), and 3.4(b) with respect to the Plan Year.

(b) During Plan Year. At any time during a Plan Year, the Administrator may determine that an individual who becomes a Qualified Employee after the first day of a Plan Year is eligible to defer Base Salary pursuant to Sections 3.2(a), 3.3(a) and 3.4(a) and Bonus pursuant to Sections 3.2(b), 3.3(b), and 3.4(b) with respect to the remainder of the Plan Year.

(c) Annual Determination. The fact that an individual has been eligible to make deferral elections with respect to any particular Plan Year does not give the individual any right to make deferral elections with respect to any other Plan Year.

2.2 Loss of Eligibility.

(a) Reasons.

(i) Ceasing to be Qualified Employee. An Active Participant will cease to be eligible to defer Base Salary and Bonus as of the date on which he or she ceases to be a Qualified Employee.

(ii) Unforeseeable Emergency. A Participant who, pursuant to Section 4.1(a), has received a distribution due to an Unforeseeable Emergency, is not eligible to defer Base Salary or Bonus with respect to the remainder of the Plan Year during which the revocation occurs or the distribution is received, as the case may be, and the immediately following Plan Year.

(iii) 401(k) Hardship Withdrawal. A Qualified Employee who receives a hardship withdrawal from a 401(k) plan maintained by a Participating Employer, or by any other employer required to be aggregated with the Participating Employer under Code section 414(b), (c), (m) or (o), is not eligible to defer Base Salary or Bonus under the Plan to the extent required to comply with the terms of the 401(k) Plan. For each Plan Year during which a deferral is not permitted, the deferral election is cancelled through the end of the Plan Year, with any new election subject to the deferral election requirements of Sections 3.2, 3.3, and 3.4

(b) Affect on Deferral Elections. An Active Participant’s deferral election for a Plan Year is irrevocable after the latest day on which the election may be made except in the event of a distribution under Section 2.2(a)(ii) or on account of a 401(k) hardship withdrawal under Section 2.2(a)(iii).

2.3 Transfer Among Participating Employers.

An Active Participant who transfers employment from one Participating Employer to another Participating Employer and who continues to be a Qualified Employee after the transfer will, for the duration of the Plan Year during which the transfer occurs, continue to participate in the Plan, in accordance with the election in effect for the portion of the Plan Year before the transfer, as a Qualified Employee of such other Participating Employer. In addition, an Active Participant who transfers to an Affiliate of a Participating Employer will, for the duration of the Plan Year during which the transfer occurs, continue to participate in Participant deferral Credits pursuant to Sections 3.2, 3.3, and 3.4 in accordance with the Active Participant's election in effect before the transfer.

2.4 Multiple Employment.

An Active Participant who is simultaneously employed as a Qualified Employee with more than one Participating Employer will participate in the Plan as a Qualified Employee of all such Participating Employers on the basis of a single deferral election pursuant to Sections 3.2, 3.3, or 3.4 applied ratably to his or her Base Salary or Bonus from each Participating Employer if his or her deferral election was made in a dollar amount or applied separately to his or her Base Salary or Bonus from each Participating Employer if his or her deferral election was made in a percentage.

2.5 Conditions of Participation.

Each Qualified Employee, as a condition of participation in the Plan, is bound by all the terms and conditions of the Plan and the Plan Rules, and must furnish to the Administrator such pertinent information and execute such election forms and other instruments as the Administrator or Plan Rules may require by such dates as the Administrator or Plan Rules may establish. All elections, directions, designations and similar actions required in connection with the Plan must be made in accordance with and are subject to the terms of the Plan and Plan Rules.

2.6 Termination of Participation.

A Participant will cease to be such as of the date on which he or she is not then eligible to make deferrals and his or her entire vested Account balances have been distributed.

ARTICLE 3.
BENEFITS

3.1 Participant Accounts.

(a) Participant Accounts. For each Participant, the Administrator will establish and maintain one or more separate bookkeeping accounts as follows:

(i) deferrals elected by the Participant pursuant to Section 3.2 will be credited to his or her Savings Account;

(ii) deferrals elected by the Participant pursuant to Section 3.3 will be credited to his or her Fixed Period (Strategy 1) Account that includes a subaccount established and maintained for the Participant in connection with each deferral election made pursuant to Section 3.3;

(iii) deferrals elected by the Participant pursuant to Section 3.4 will be credited to his or her Fixed Period (Strategy 2) Account that includes a subaccount established and maintained for the Participant in connection with each deferral election made pursuant to Section 3.4; and

(iv) credits made on the Participant's behalf (if any) pursuant to Section 3.5 will be credited to his or her Retirement Account.

3.2 Participant Deferral Credits – Savings Account.

(a) Base Salary. Base Salary deferrals will be made in accordance with the following rules:

(i) An Active Participant may elect to defer his or her Base Salary for a Plan Year from a minimum percentage or dollar amount to a maximum percentage or dollar amount, as specified in Plan Rules. Plan Rules may specify minimum and maximum deferral amounts for a Plan Year, any period within a Plan Year or both.

(ii) An election made pursuant to this subsection will not be effective unless it is made on a properly completed election form received by the Administrator by a date specified by the Administrator which is prior to the first day of the Plan Year to which the election relates or, in the case of an individual who becomes eligible to participate after the first day of a Plan Year, within 30 days after he or she becomes eligible to participate. The special 30-day rule is only applicable to an individual who during the preceding 24-month period was not eligible to participate in this Plan or any other non-qualified deferred compensation plan maintained by the Company or an Affiliate that is required to be treated as a single plan with the Plan under Code Section 409A.

(iii) Intentionally omitted.

(iv) Any election pursuant to this subsection applies only to Base Salary relating to services performed after the effective date of the election.

(v) One-Time Election. In connection with the amendment of the plan to add the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account options under Sections 3.3 and 3.4, an Active Participant may revoke or modify his or her election under this Subsection (a) for the period from April 1, 2003 to December 31, 2003 and elect to defer Base Salary pursuant to Section 3.3 or Section 3.4 for the period from April 1, 2003 to December 31, 2003 by submitting a properly completed election form to the Administrator by March 31, 2003.

(b) Bonus. Bonus deferrals will be made in accordance with the following rules:

(i) An Active Participant may elect to defer all or any portion of his or her Bonus for the Plan Year from a minimum percentage or dollar amount to a maximum percentage or dollar amount, as specified in Plan Rules.

(ii) An election made by an Active Participant pursuant to this subsection will not be effective unless it is made on a properly completed election form received by the Administrator prior to the first day of the Plan Year to which the election relates and shall apply to the bonus that relates solely to services performed on or after the beginning of such Plan Year.

(iii) Intentionally omitted.

(iv) Notwithstanding the foregoing provisions of this Subsection (b), an Active Participant may elect to defer all or any portion of his or her Bonus that is to be determined and paid to such Active Participant in 2003, by submitting a properly completed election form to the Administrator by December 20, 2002.

(c) Limitations. The Administrator may, prior to the effective date of a Participant's election, limit the amount of the Participant's deferral to be made under this section to account for other anticipated payroll deductions. In addition, Plan Rules may specify individual or aggregate annual or lifetime deferral limitations.

(d) Allocation to Savings Account. An Active Participant's deferrals pursuant to this section will be allocated to his or her Savings Account.

(e) Timing of Credits. Deferrals of an Active Participant's Base Salary and Bonus pursuant to this section will be credited to his or her Savings Account as of the date on which the Participant would have otherwise received the Base Salary or Bonus but for his or her deferral election pursuant to this section.

3.3 Participant Deferral Credits – Fixed Period (Strategy 1) Account.

(a) Base Salary. Base Salary deferrals will be made in accordance with the following rules:

(i) An Active Participant may elect to defer his or her Base Salary for a Plan Year from a minimum percentage or dollar amount to a maximum percentage or dollar amount, as specified in Plan Rules. Plan Rules may specify minimum and maximum deferral amounts for a Plan Year, any period within a Plan Year or both.

(ii) An election made pursuant to this subsection will not be effective unless it is made on a properly completed election form received by the Administrator by a date specified by the Administrator which is prior to the first day of the Plan Year to which the election relates or, in the case of an individual who becomes eligible to participate after the first day of a Plan Year, within 30 days after he or she becomes eligible to participate. The special 30-day rule is only applicable to an individual who during the preceding 24-month period was not eligible to participate in this Plan or any other non-qualified deferred compensation plan maintained by the Company or an Affiliate that is required to be treated as a single plan with the Plan under Code Section 409A.

(iii) Intentionally omitted.

(iv) Any election pursuant to this subsection applies only to Base Salary relating to services performed after the effective date of the election.

(b) Bonus. Bonus deferrals will be made in accordance with the following rules:

(i) An Active Participant may elect to defer all or any portion of his or her Bonus for the Plan Year from a minimum percentage or dollar amount to a maximum percentage or dollar amount, as specified in Plan Rules.

(ii) An election made by an Active Participant pursuant to this subsection will not be effective unless it is made on a properly completed election form received by the Administrator prior to the first day of the Plan Year to which the election relates and shall apply to the Bonus that relates solely to services performed on or after the beginning of such Plan Year.

(c) Limitations. The Administrator may, prior to the effective date of an Active Participant's election, limit the amount of the Active Participant's deferral to be made under this section to account for other anticipated payroll deductions. In addition, Plan Rules may specify individual or aggregate annual or lifetime deferral limitations.

(d) Allocation to Fixed Period (Strategy 1) Account and Subaccounts. An Active Participant's deferrals pursuant to this section will be allocated to his or her Fixed

Period (Strategy 1) Account. Each election made under Subsection (a) or Subsection (b) for a particular Plan Year will be credited to a subaccount.

(e) Timing of Credits. Deferrals of an Active Participant's Base Salary and Bonus pursuant to this section will be credited to his or her Fixed Period (Strategy 1) Account as of the date on which the Participant would have otherwise received the Base Salary or Bonus but for his or her deferral election pursuant to this section.

(f) 2003 Deferral Election. In connection with the amendment of the Plan to add the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account options under Sections 3.3 and 3.4, an Active Participant may elect to defer Base Salary pursuant to Subsection (a) for the period from April 1, 2003 to December 31, 2003, by submitting a properly completed election form to the Administrator by March 31, 2003.

(g) One-Time Transfer Election. In connection with the amendment of the Plan to add the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account options under Sections 3.3 and 3.4, an Active Participant may, no later than April 1, 2003, transfer all or a portion of the vested balance of his or her Savings Account to his or her Fixed Period (Strategy 1) Account or Fixed Period (Strategy 2) Account; provided that the distribution of such transferred vested balance will not be distributed to the Participant earlier than January 1, 2006. Notwithstanding the foregoing, if the Participant's Termination Date is in 2003 or 2004 distribution of any amount transferred pursuant to this paragraph (g), plus earnings credited to such amount, will be made in a lump sum payment pursuant to the provisions of Section 4.2.

(h) One-Time Change to Distribution Election of Fixed Period Accounts. Due to an administrative error in communicating the distribution options available to a Participant who elects to defer Base Salary or Bonus pursuant to the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account options under Sections 3.3 and 3.4, an Active Participant will be allowed to make a one-time election to modify the distribution election(s) the Participant made with respect to any subaccount established under the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account for the period from April 1, 2003 to December 31, 2003 and the period from January 1, 2004 to December 31, 2004. In addition to the original distribution election the Participant made for any such subaccount, an Active Participant may elect whether, in the event the Participant has not received a distribution of the entire balance of such subaccount as of his or her Termination Date, to receive distribution of the entire balance of such subaccount in a single lump sum payment as soon as administratively practicable after the last day of the Plan Year that includes the Participant's Termination Date. An Active Participant may make an election pursuant to this section by submitting a properly completed election form to the Administrator by March 31, 2004.

3.4 Participant Deferral Credits – Fixed Period (Strategy 2) Account.

(a) Base Salary. Base Salary deferrals will be made in accordance with the following rules:

(i) An Active Participant may elect to defer his or her Base Salary for a Plan Year from a minimum percentage or dollar amount to a maximum percentage or dollar amount, as specified in Plan Rules. Plan Rules may specify minimum and maximum deferral amounts for a Plan Year, any period within a Plan Year or both.

(ii) An election made pursuant to this subsection will not be effective unless it is made on a properly completed election form received by the Administrator by a date specified by the Administrator which is prior to the first day of the Plan Year to which the election relates or, in the case of an individual who becomes eligible to participate after the first day of a Plan Year, within 30 days after he or she becomes eligible to participate. The special 30-day rule is only applicable to an individual who during the preceding 24-month period was not eligible to participate in this Plan or any other non-qualified deferred compensation plan maintained by the Company or an Affiliate that is required to be treated as a single plan with the Plan under Code Section 409A.

(iii) Intentionally omitted.

(iv) Any election pursuant to this subsection applies only to Base Salary relating to services performed after the effective date of the election.

(b) Bonus. Bonus deferrals will be made in accordance with the following rules:

(i) An Active Participant may elect to defer all or any portion of his or her Bonus for the Plan Year from a minimum percentage or dollar amount to a maximum percentage or dollar amount, as specified in Plan Rules.

(ii) An election made by an Active Participant pursuant to this subsection will not be effective unless it is made on a properly completed election form received by the Administrator prior to the first day of the Plan Year to which the election relates and shall apply to the Bonus that relates solely to services performed on or after the beginning of such Plan Year.

(iii) Intentionally omitted.

(c) Limitations. The Administrator may, prior to the effective date of a Participant's election, limit the amount of the Participant's deferral to be made under this section to account for other anticipated payroll deductions. In addition, Plan Rules may specify individual or aggregate annual or lifetime deferral limitations.

(d) Allocation to Fixed Period (Strategy 2) Account. An Active Participant's deferrals pursuant to this section will be allocated to his or her Fixed Period (Strategy 2) Account. Each election made under Subsection (a) or Subsection (b) for a particular Plan Year will be credited to a subaccount.

(e) Timing of Credits. Deferrals of an Active Participant's Base Salary and Bonus pursuant to this section will be credited to his or her Fixed Period (Strategy 2) Account as of the date on which the Participant would have otherwise received the Base Salary or Bonus but for his or her deferral election pursuant to this section.

(f) 2003 Deferral Election. In connection with the amendment of the Plan to add the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account options under Sections 3.3 and 3.4, an Active Participant may elect to defer Base Salary pursuant to Subsection (a) for the period from April 1, 2003 to December 31, 2003, by submitting a properly completed election form to the Administrator by March 31, 2003.

(g) One-Time Transfer Election. In connection with the amendment of the Plan to add the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account options under Sections 3.3 and 3.4, an Active Participant may, no later than April 1, 2003, transfer all or a portion of the vested balance of his or her Savings Account to his or her Fixed Period (Strategy 1) Account or Fixed Period (Strategy 2) Account; provided that the distribution of such transferred vested balance will not be distributed to the Participant earlier than January 1, 2006. Notwithstanding the foregoing, if the Participant's Termination Date is in 2003 or 2004 distribution of any amount transferred pursuant to this paragraph (g), plus earnings credited to such amount, will be made in a lump sum payment pursuant to the provisions of Section 4.2.

(h) One-Time Change to Distribution Election of Fixed Period Accounts. Due to an administrative error in communicating the distribution options available to a Participant who elects to defer Base Salary or Bonus pursuant to the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account options under Sections 3.3 and 3.4, an Active Participant will be allowed to make a one-time election to modify the distribution election(s) the Participant made with respect to any subaccount established under the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account for the period from April 1, 2003 to December 31, 2003 and the period from January 1, 2004 to December 31, 2004. In addition to the original distribution election the Participant made for any such subaccount, an Active Participant may elect whether, in the event the Participant has not received a distribution of the entire balance of such subaccount as of his or her Termination Date, to receive distribution of the entire balance of such subaccount in a single lump sum payment as soon as administratively practicable after the last day of the Plan Year that includes the Participant's Termination Date. An Active Participant may make an election pursuant to this section by submitting a properly completed election form to the Administrator by March 31, 2004.

3.5 Participating Employer Credits.

A Participating Employer may from time to time credit the Retirement Account of any Participant with an amount determined by the Participating Employer. If a Participating Employer chooses to make such a credit, the Company will provide the Participant with a written notice that specifies the amount of the credit, the timing of the credit and, any conditions that the Participant must satisfy to be entitled to the credit. Credits pursuant to this subsection will be made, if at all, on a Participant-by-Participant basis. If a Participating Employer chooses to credit the Retirement Account of a Participant pursuant to this subsection, the Participating Employer is not, as a result, required to make any credit to the Retirement Account of any other Participant, whether or not he or she is otherwise similarly situated.

3.6 Earnings Credits.

(a) Designation of Investment Funds. The Administrator will designate two or more investment funds that will serve as the basis for determining adjustments pursuant to this section. The Administrator may, from time to time, designate additional investment funds or eliminate any previously designated investment funds. The designation or elimination of a fund pursuant to this subsection is not a Plan amendment. The Administrator will not be responsible in any manner to any Participant or other person for any damages, losses, liabilities, costs or expenses of any kind arising in connection with any designation or elimination of an investment fund.

(b) Participant Direction. A Participant must direct the manner in which amounts credited to his or her Accounts pursuant to Sections 3.2, 3.3, 3.4 or 3.5 will be deemed to be invested among the investment funds designated pursuant to Subsection (a). Amounts will be deemed to be invested in accordance with the Participant's direction on or as soon as administratively practicable after the amounts are credited to the Participant's Account. To the extent a Participant fails to direct the manner in which amounts credited to his or her Accounts will be deemed to be invested, such amounts will deemed to be invested in the manner specified in Plan Rules.

(c) Change in Direction for Future Credits. A Participant may direct a change in the manner in which future credits to his or her Accounts pursuant to Sections 3.2, 3.3, 3.4 or 3.5 will be deemed to be invested among the investment funds designated pursuant to Subsection (a). The direction will be effective for deferrals credited to the Participant's Account pursuant to Sections 3.2, 3.3, 3.4 or 3.5 at least 30 days (or such shorter period as Plan Rules may allow) after the date on which the Administrator receives the direction from the Participant.

(d) Change in Direction for Existing Account Balance. A Participant may direct a change in the manner in which his or her existing Account balances are deemed to be invested among the investment funds designated pursuant to Subsection (a).

The direction will be effective as soon as administratively practicable after the date on which the Administrator receives the direction from the Participant.

(e) Account Adjustment. As of the close of business on each day on which the New York Stock Exchange is open for regular business, the Administrator will cause Participants' Accounts to be separately adjusted, in a manner determined by the Administrator to be uniform and equitable, to reflect the income, expense, gains, losses, fees and the like (other than taxes) that would have resulted since the last adjustment had the Participant's investment directions pursuant to this section actually been implemented. For purposes of this subsection, an amount will be deemed to have been invested in accordance with a Participant's direction by the fifth business day after (i) the date on which the amount is credited to the Participant's Account in the case of a direction pursuant to Subsection (b) or Subsection (c) or (ii) the effective date of a direction pursuant to Subsection (d). To the extent determined by the Administrator to be necessary in conjunction with any distribution pursuant to the Plan, the Administrator will cause the Account from which the distribution is to be made to be adjusted to reflect a good faith estimate by the Administrator of any fees and other expenditures payable after the date of the distribution in connection with deemed investment activity in the Account through and including the date of the distribution. Any such estimate is binding on the Participating Employer and the person to whom the distribution is made.

(f) Obligations and Responsibilities of Administrator. The sole obligation of the Administrator with respect to the designation or elimination of any investment fund designated pursuant to Subsection (a) is to act in accordance with the express terms of Subsection (a). By way of example and without limiting the previous sentence, the Administrator is not required, and no course of conduct will cause it to be required, to investigate or monitor any designated fund to any extent or for any purpose or to take or refrain from taking any action with respect to a fund because of any aspect of the performance of the fund. The designation of a limited number of investment funds is solely for administrative convenience and in no way reflects any endorsement of any such funds by the Administrator.

(g) Deemed Investment. Trust assets are not required to be invested in accordance with a Participant's directions and the balance of all Accounts pursuant to the Plan will be determined pursuant to this section and other applicable sections of the Plan without regard to the actual amount of Trust assets.

(h) Participant Responsibilities. Each Participant is solely responsible for any and all consequences of his or her investment directions made pursuant to this section. Neither any Participating Employer, any of its directors, officers or employers, the Company's Board nor the Administrator has any responsibility to any Participant or other person for any damages, losses, liabilities, costs or expenses of any kind arising in connection with any investment direction made by a Participant pursuant to this section.

3.7 Vesting.

(a) Each Participant always has a fully vested nonforfeitable interest in his or her Savings Account, Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account.

(b) A Participant will acquire a fully vested nonforfeitable interest in his or her Retirement Account if he or she dies or becomes disabled on or prior to his or her Termination Date.

(c) A Participant whose Retirement Account is not otherwise fully vested will acquire a vested nonforfeitable interest in the portion of his or her Retirement Account to the extent provided in the following schedule based on the Participant's Years of Service:

Full Years of Service	Vested Interest
Less than One Year	0%
At least One Year	25%
At least Two Years	50%
At least Three Years	75%
Four or More Years	100%

ARTICLE 4.
DISTRIBUTION

4.1 Distribution to Participant Before Severance or Disability.

(a) Withdrawals Due to Unforeseeable Emergency. Prior to a Participant's Termination Date, a distribution will be made to a Participant from his or her vested Accounts if the Participant submits a written distribution request to the Administrator and the Administrator determines that the Participant has experienced an Unforeseeable Emergency. The amount of the distribution may not exceed the lesser of (i) the amount necessary to satisfy the emergency, as determined by the Administrator or (ii) the vested balance of the Accounts. The distribution will be made in the form of a lump sum cash payment as soon as administratively practicable (but not more than 90 days) after the Administrator's determination that the Participant has experienced an Unforeseeable Emergency. Any distribution pursuant to this subsection will be made in the following order: first, from the Participant's Savings Account; second, from his or her Fixed Period (Strategy 1) Account; third, from his or her Fixed Period (Strategy 2) Account; and fourth, from his or her Retirement Account.

(b) Reduction of Account Balance. The balances of a Participant's Accounts will be reduced (but not below zero) by the amount of the distribution as of the date of the distribution.

4.2 Distribution of Savings and Retirement Accounts to Participant After Termination Date.

(a) Time. Distribution to a Participant of the vested balance of his or her Savings and Retirement Accounts will be made or commence as soon as administratively practicable (but not more than 90 days) after the Participant's Termination Date.

(b) Form. Distribution to the Participant of the vested balance of his or her Savings and Retirement Accounts will be made in the form of a single lump sum cash payment unless the Participant has made a written election to receive his or her distribution in the form of ten annual installment cash payments on a properly completed election form filed with the Administrator at the time of his or her written elections to defer Base Salary or Bonus pursuant to Section 3.2.

(c) Amount.

(i) Lump Sum. The amount of a lump sum payment from a Participant's Savings and Retirement Accounts will be equal to the vested balances of the Accounts.

(ii) Installments. The amount of an installment payment from a Participant's Savings and Retirement Accounts will be determined by dividing the vested balances of the Savings and Retirement Accounts by the total number of remaining payments (including the current payment). The undistributed portion of a Savings or Retirement Account distributed in the form of installment payments will continue to be credited with earnings in accordance with Section 3.6.

(d) Reduction of Account Balances. The balance of the Accounts will be reduced (but not below zero) by the amount of the distribution as of the date of the distribution.

4.3 Distribution of Fixed Period (Strategy 1) and Fixed Period (Strategy 2) Accounts to Participant.

(a) Time. Distribution to a Participant of the vested balance of each of his or her subaccounts under the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account will be made or commence on the dates elected by the Participant at the time of his or her written elections to defer Base Salary or Bonus pursuant to Section 3.3. or 3.4.

(b) Form. Distribution to the Participant of the vested balance of his or her subaccounts under the Fixed Period (Strategy 1) Account or Fixed Period (Strategy 2) Account will be made in the form of a lump sum cash payment or in the form of four annual installment cash payments, as elected by the Participant at the time of his or her written election to defer Base Salary or Bonus pursuant to Section 3.3 or 3.4.

(c) Amount.

(i) Lump Sum. The amount of a lump sum payment from a Participant's subaccount under the Fixed Period (Strategy 1) Account or Fixed Period (Strategy 2) Account will be equal to the vested balance of the subaccount.

(ii) Installments. The amount of an installment payment from a Participant's subaccount under the Fixed Period (Strategy 1) Account or Fixed Period (Strategy 2) Account will be determined by dividing the vested balance of the subaccount under the Fixed Period (Strategy 1) Account or Fixed Period (Strategy 2) Account, as the case may be, by the total number of remaining payments (including the current payment). The undistributed portion of a subaccount distributed in the form of installment payments will continue to be credited with earnings in accordance with Section 3.6.

(d) Reduction of Subaccount Balances. The balance of a subaccount under the Fixed Period (Strategy 1) Account and Fixed Period (Strategy 2) Account will be reduced (but not below zero) by the amount of the distribution as of the date of the distribution.

4.4 Distribution to Beneficiary.

(a) Time. Distribution to a Beneficiary will be made as soon as administratively practicable (but not more than 90 days) after the Participant's death.

(b) Form. Distribution to the Beneficiary will be made in the form of a lump sum cash payment whether or not payments had commenced to the Participant in the form of installments prior to his or her death.

(c) Amount. The amount of a lump sum payment will be equal to the balance of the deceased Participant's Accounts.

(d) Reduction of Account Balance. The balances of the Accounts will be reduced (but not below zero) by the amount of the distribution as of the date of the distribution.

(e) Beneficiary Designation.

(i) Each Participant may designate, on a form furnished by the Administrator, one or more primary Beneficiaries or alternative Beneficiaries to receive all or a specified part of his or her Accounts after his or her death, and the Participant may change or revoke any such designation from time to time. No such designation, change or revocation is effective unless executed by the Participant and received by the Administrator during the Participant's lifetime.

(ii) If a Participant—

(1) fails to designate a Beneficiary, or

(2) revokes a Beneficiary designation without naming another Beneficiary, or

(3) designates one or more Beneficiaries, none of whom survives the Participant or exists at the time in question,

for all or any portion of his or her Account, such Account or portion will be paid to the Participant's surviving spouse or, if the Participant is not survived by a spouse, to the representative of the Participant's estate.

(iii) The automatic Beneficiaries specified above and, unless the designation otherwise specifies, the Beneficiaries designated by the Participant, become fixed as of the Participant's death so that, if a Beneficiary survives the Participant but dies before the receipt of the payment due such Beneficiary, the payment will be made to the representative of such Beneficiary's estate. Any designation of a Beneficiary by name that is accompanied by a description of relationship or only by statement of relationship to the Participant is effective only to designate the person or persons standing in such relationship to the Participant at the Participant's death.

4.5 Nondeductibility.

If the Company determines in good faith that there is a reasonable likelihood that any compensation paid to a Participant by an Affiliate for a taxable year of the Affiliate would not be deductible by the Affiliate solely by reason of the limitation under Code section 162(m), to the extent deemed necessary by the Company to ensure that the entire amount of any distribution to the Participant pursuant to the Plan is deductible, notwithstanding any other provision of the Plan or any election by the Participant to the contrary, all or any portion of the distribution may be deferred. Any amounts deferred pursuant to this section will continue to be credited with earnings in accordance with Section 3.6. The deferred amounts and earnings thereon will be distributed to the Participant, or to his or her Beneficiary in the case of the Participant's death, at the earliest possible date, as determined by the Company in good faith, on which the deductibility of compensation paid or payable to the Participant for the taxable year of the Affiliate during which the distribution is made will not be limited by Code section 162(m).

4.6 Payment in Event of Incapacity.

If any individual entitled to receive any payment under the Plan is, in the judgment of the Administrator, physically, mentally or legally incapable of receiving or acknowledging receipt of the payment, and no legal representative has been appointed for the individual, the Administrator may (but is not required to) cause the payment to be made to any one or more of the following as may be chosen by the Administrator: the Beneficiary (in the case of the incapacity of a Participant); the institution maintaining the individual; a custodian for the individual under the Uniform Transfers to Minors Act of any state; or the individual's spouse, children, parents, or other relatives by blood or marriage. The Administrator is not required to see to the proper application of any such payment and the payment completely discharges all claims under the Plan against the Participating Employer, the Plan and Trust to the extent of the payment.

4.7 Five-Year Redeferral Election.

Notwithstanding Section 4.2, on or after January 1, 2009, a Participant may elect to change the form of his or her distribution or delay the commencement date specified in a prior distribution election. An election pursuant to this Section will not have any effect unless the election (a) is made on a properly completed form received by the Administrator at least twelve (12) months prior to the date that the Participant's scheduled payment was to begin, (b) is not effective until at least twelve (12) months after the date on which the election is made, and (c) delays the payment at least five (5) years beyond the distribution date originally specified. An election under this Section 4.7 will not change the form or time of distribution upon the Participant's death as provided under Section 4.4

4.8 Transition Period Election.

Notwithstanding any provisions of this Plan to the contrary, during calendar year 2008, the Company may, at the time and in the manner prescribed by Plan Rules, permit a Participant (who is not classified by the Company as a Senior Vice President or higher) to elect to receive a distribution on a fixed date or dates not earlier than January 1, 2009, of all or a portion of the Participant's Accounts, including any remaining installment distributions payable after 2008, provided, however, such election shall not apply to any amounts the Participant has designated as being deemed to be invested in Company stock.

4.9 Installment Distributions

With respect to any installment distribution, for purposes of Code Section 409A, each installment payment shall be considered a separate payment.

4.10 Six-Month Suspension for Specified Employees

If a Participant is a Specified Employee on his or her Termination Date, distribution under this Plan made on account of such Participant's Termination of Employment will be suspended and not made on until the first date following the end of the six-month period following the Participant's Termination Date. For this purpose, a 'Specified Employee' means a Participant who, on his or her Termination Date, is a 'key employee' (as defined below), and the Company or an Affiliate has stock that is traded on an established securities market (within the meaning of Code Section 409A(a)(2)(B)). The Participant is a 'key employee' during the 12-month period beginning on the April 1 immediately following a calendar year at any time during which such Participant was a key employee as defined in Code Section 416(i) (without regard to Code Section 416(i)(5)) of the Company or an Affiliate. A Participant will not be treated as a Specified Employee if he or she would not be a 'specified employee' as defined under Treasury regulations issued under Code Section 409A.

ARTICLE 5.
SOURCE OF PAYMENTS; NATURE OF INTEREST

5.1 Establishment of Trust.

Each Participating Employer will establish a Trust, or become covered by a Trust established by another Participating Employer, with an independent corporate trustee. The Trust must (a) be a grantor trust with respect to which the Participating Employer is treated as the grantor for purposes of Code section 677, (b) not cause the Plan to be funded for purposes of Title I of ERISA and (c) provide that the Trust assets will, upon the insolvency of a Participating Employer, be used to satisfy claims of the Participating Employer's general creditors. The Participating Employers may from time to time transfer to the Trust cash, marketable securities or other property acceptable to the Trustee in accordance with the terms of the Trust. The Participating Employers will pay all taxes of any kind whatsoever payable in respect of Trust assets or any transaction with respect to Trust assets, other than taxes payable by a Participant or Beneficiary, or any other person claiming by, under or through a Participant or Beneficiary, in connection with a distribution from the Plan.

5.2 Source of Payments.

(a) Each Participating Employer will pay, from its general assets, the portion of any benefit pursuant to Article 4 or Section 6.3 or 6.4 attributable to a Participant's Accounts with respect to that Participating Employer, and all costs, charges and expenses relating thereto.

(b) The Trustee will make distributions to Participants and Beneficiaries from the Trust in satisfaction of a Participating Employer's obligations under the Plan in accordance with the terms of the Trust. The Participating Employer is responsible for paying any benefits attributable to a Participant's Account with respect to that Participating Employer that are not paid by the Trust.

5.3 Status of Plan.

Nothing contained in the Plan or Trust is to be construed as providing for assets to be held for the benefit of any Participant or any other person or persons to whom benefits are to be paid pursuant to the terms of this Plan, the Participant's or other person's only interest under the Plan being the right to receive the benefits set forth herein. The Trust is established only for the convenience of the Participating Employers and the Participants, and no Participant has any interest in the assets of the Trust prior to distribution of such assets pursuant to the Plan. To the extent the Participant or any other person acquires a right to receive benefits under this Plan or the Trust, such right is no greater than the right of any unsecured general creditor of the Participating Employer.

5.4 Non-assignability of Benefits.

The benefits payable under the Plan and the right to receive future benefits under the Plan may not be anticipated, alienated, sold, transferred, assigned, pledged, encumbered, or subjected to any charge or legal process.

ARTICLE 6.
AMENDMENT, TERMINATION

6.1 Adoption.

With the prior approval of the Administrator, an Affiliate may adopt the Plan and become a Participating Employer by furnishing to the Administrator a certified copy of a resolution of its Board adopting the Plan.

6.2 Amendment.

(a) Right. The Company reserves the right to amend the Plan at any time to any extent that it may deem advisable.

(b) Method. To be effective, an amendment must be stated in a written instrument approved in advance or ratified by the Company's Board and executed in the name of the Company by two of its officers.

(c) Binding Effect. An amendment adopted in accordance with Subsection (b) is binding on all interested parties as of the effective date stated in the amendment; provided, however, that no amendment may retroactively deprive any Participant, or the Beneficiary of a deceased Participant, of any benefit to which he or she is entitled under the terms of the Plan in effect immediately prior to the effective date of the amendment or the date on which the amendment is adopted, whichever is later.

(d) Certain Amendments to Earnings Credit Method. Any amendment that materially changes the method of determining the adjustments to Participants' Accounts pursuant to Section 3.6 is effective with respect to the portion of the Accounts attributable to credits made before the date on which the amendment is adopted only if the Company's Board determines in good faith that on that date, it is reasonably likely that, in the long run, the new method will not result in materially lower credit rate than the old method.

(e) Applicability to Participants Who Have Terminated Employment. The provisions of the Plan in effect on a Participant's Termination Date will, except as otherwise expressly provided by a subsequent amendment, continue to apply to such Participant.

6.3 Termination of Participation.

Notwithstanding any other provision of the Plan to the contrary, if determined by the Administrator to be necessary to ensure that the Plan is exempt from ERISA to the extent contemplated by Section 1.3, or upon the Administrator's determination that a Participant's interest in the Plan has been or is likely to be includable in the Participant's gross income for federal income tax purposes prior to the actual payment of benefits pursuant to the Plan, the Administrator may take any or all of the following steps:

(a) terminate the Participant’s future participation in the Plan;

(b) cause the Participant’s entire vested interest in the Plan to be distributed to the Participant in the form of an immediate lump sum cash payment; and/or

(c) transfer the benefits that would otherwise be payable pursuant to the Plan for all or any of the Participants to a new plan that is similar in all material respects (other than those which require the action in question to be taken).

6.4 Termination.

The Company reserves the right to terminate the Plan in its entirety at any time. Each Participating Employer reserves the right to cease its participation in the Plan at any time. The Plan will terminate in its entirety or with respect to a particular Participating Employer as of the date specified by the Company or such Participating Employer in a written instrument adopted in the same manner as an amendment. Upon the termination of the Plan in its entirety or with respect to any Participating Employer, the Company or Participating Employer, as the case may be, will either cause (a) any benefits to which Participants have become entitled prior to the effective date of the termination to continue to be paid in accordance with the provisions of Article 4 or (b) the vested Account balances of any or all Participants, or the Beneficiaries of any or all deceased Participants, to be distributed in the form of an immediate lump sum payment. In all cases distribution shall be made in accordance with and subject to the requirements of Code section 409A.

ARTICLE 7.
DEFINITIONS, CONSTRUCTION AND INTERPRETATION

7.1 <u>Cross Reference</u>.

References within a section of the Plan to a particular subsection refer to that subsection within the same section and references within a section or subsection to a particular clause refer to that clause within the same section or subsection, as the case may be. The definitions and rules of construction and interpretation set forth in this article apply in construing the Plan unless the context otherwise indicates.

7.2 <u>Governing Law</u>.

To the extent that state law is not preempted by the provisions of ERISA, or any other laws of the United States, all questions pertaining to the construction, validity, effect and enforcement of the Plan will be determined in accordance with the internal, substantive laws of the State of Minnesota without regard to the conflict of law rules of the State of Minnesota or any other jurisdiction.

7.3 <u>Headings</u>.

The headings of articles and sections are included solely for convenience of reference; if there exists any conflict between such headings and the text of the Plan, the text will control.

7.4 <u>Number and Gender</u>.

Wherever appropriate, the singular may be read as the plural, the plural may be read as the singular and one gender may be read as the other gender.

7.5 <u>Definitions</u>.

The terms in this section when used with initial capitalization have the following meanings, unless the context otherwise indicates.

<u>Account</u>. “Account” means the bookkeeping account maintained with respect to a Participant pursuant to Section 3.1 and may mean the Savings Account, Fixed Period (Strategy 1) Account, Fixed Period (Strategy 2) Account, or Retirement Account or all of them, as the context requires.

<u>Active Participant</u>. “Active Participant” with respect to a Plan Year means a Qualified Employee who is eligible to make deferrals pursuant to the Plan for the Plan Year, for the portion of the Plan Year during which he or she remains eligible.

<u>Administrator</u>. “Administrator” means the Company or the person to whom administrative duties are delegated pursuant to the provisions of Section 8.1, as the context requires.

<u>Affiliate</u>. “Affiliate” means the Company and any other company or trade or business, whether or not incorporated, that together with the Company is treated as a single employer pursuant to Code section 414(b) or 414(c).

Base Salary. “Base Salary” for a Plan Year means the base salary payable in cash to an Active Participant by a Participating Employer for the Participant’s services during the Plan Year as a Qualified Employee, net of any contributions or deductions specified in Plan Rules.

Beneficiary. “Beneficiary” with respect to a Participant is the person designated or otherwise determined under the provisions of Section 4.4(e) as the distributee of benefits payable after the Participant’s death. A person designated or otherwise determined to be a Beneficiary under the terms of the Plan has no interest in or right under the Plan until the Participant in question has died. A Beneficiary will cease to be such on the day on which all benefits to which he, she or it is entitled under the Plan have been distributed.

Board. “Board” means the board of directors of the Affiliate in question. When the Plan provides for an action to be taken by the Board, the action may be taken by any committee or individual authorized to take such action pursuant to a proper delegation by the board of directors in question.

Bonus. “Bonus” for a Plan Year means the annual bonus earned by an Active Participant during the Plan Year for his or her services during the Plan Year as a Qualified Employee and paid in cash to the Participant by a Participating Employer during the Plan Year first following the Plan Year, net of any contributions or deductions specified in Plan Rules.

Code. “Code” means the Internal Revenue Code of 1986, as amended. Any reference to a specific provision of the Code includes a reference to that provision as it may be amended from time to time and to any successor provision.

Company. “Company” means Select Comfort Corporation, a Minnesota corporation.

Disabled. A Participant will be considered to be ‘Disabled’ only if the Participant, by reason of any medically determinable physical or mental impairment that can be expected to result in death or can be expected to last for a continuous period of not less than 12 months (i) is unable to engage in any substantial gainful activity, (ii) is receiving income replacement benefits for a period of not less than three months under an accident and health plan covering employees of the Company or an Affiliate, or (iii) is determined to be totally disabled by the Social Security Administration; provided, however, in all cases the Employee is considered ‘Disabled’ within the meaning of Code Section 409A(a)(2)(C). The Board shall determine whether the Employee is Disabled on the basis of medical evidence satisfactory to the Board.

ERISA. “ERISA” means the Employee Retirement Income Security Act of 1974, as amended. Any reference to a specific provision of ERISA includes a reference to that provision as it may be amended from time to time and to any successor provision.

Fixed Period (Strategy 1) Account. “Fixed Period (Strategy 1) Account” with respect to a Participant means the Account and subaccounts maintained on his or her behalf pursuant to Section 3.1(a)(ii).

Fixed Period (Strategy 2) Account. “Fixed Period (Strategy 2) Account” with respect to a Participant means the Account and subaccounts maintained on his or her behalf pursuant to Section 3.1(a)(iii).

Participant. “Participant” means a current or former Active Participant to whose Account amounts have been credited pursuant to Article 3 and who has not ceased to be a Participant pursuant to Section 2.6.

Participating Employer. “Participating Employer” means the Company and any other Affiliate that has adopted the Plan, or all of them collectively, as the context requires. An Affiliate will cease to be a Participating Employer upon a termination of the Plan as to its employees and the satisfaction in full of all of its obligations under the Plan or upon its ceasing to be an Affiliate.

Plan. “Plan” means the Select Comfort Executive Investment Plan, as from time to time amended or restated.

Plan Rules. “Plan Rules” are rules, policies, practices or procedures adopted by the Administrator pursuant to Section 8.2.

Plan Year. ‘Plan Year’ means the calendar year; provided that the first Plan Year is the period beginning on December 20, 2002 and ending on December 31, 2002.

Qualified Employee. “Qualified Employee” means an individual who performs services for a Participating Employer as an employee of the Participating Employer (as classified by the Participating Employer at the time the services are performed without regard to any subsequent reclassification) and who is determined by the Administrator to be a management or highly compensated employee of the Participating Employer.

Retirement Account. “Retirement Account” with respect to a Participant means the Account maintained on his or her behalf pursuant to Section 3.1(a)(iv).

Savings Account. “Savings Account” with respect to a Participant means the Account maintained on his or her behalf pursuant to Section 3.1(a)(i).

Termination Date. “Termination Date” means the date on which a Participant has completely severed his or her employment relationship with the Participating Employer and all other Affiliates provided such termination constitutes a separation from service under Code Section 409A, or the Participant has experienced a change in his or her employment relationship that constitutes a ‘separation from service’ under Code Section 409A. A Participant’s employment will be treated as remaining intact while the Participant is on a military leave, a sick leave or other bona fide leave of absence (pursuant to which there is a reasonable expectation that the Participant will return to perform services for a Participating Employer or other Affiliate) but only if the period of such leave does not exceed six (6) months, or if longer, so long as the Participant retains a right to reemployment with a Participating Employer or other Affiliate under applicable statute or by contract.

Trust. “Trust” means any trust or trusts established by a Participating Employer pursuant to Section 5.1.

Trustee. “Trustee” means the independent corporate trustee or trustees that at the relevant time has or have been appointed to act as Trustee of the Trust.

Unforeseeable Emergency. “Unforeseeable Emergency” means an unanticipated emergency that is caused by an event beyond the Participant’s control resulting in a severe financial hardship that cannot be satisfied through other means. The existence of an unforeseeable emergency will be determined by the Administrator in its sole discretion. An Unforeseeable Emergency will exist only if and to the extent the Administrator determines that it constitutes an ‘unforeseeable emergency’ under Code Section 409A.

Years of Service. “Years of Service” for purposes of determining a Participant’s vested interest in his or her Retirement Account pursuant to Section 3.7, means the sum of a Qualified Employee’s periods of service as an employee with the Affiliates (measured in the case of any Affiliate from not earlier than the date on which it became an Affiliate), commencing as of the Qualified Employee’s employment commencement date and ending with the Qualified Employee’s Termination Date.

ARTICLE 8.
ADMINISTRATION

8.1 Administrator.

The general administration of the Plan and the duty to carry out its provisions is vested in the Company. The Company may delegate such duty or any portion thereof to a named person or persons and may from time to time revoke such authority and delegate it to another person or persons.

8.2 Plan Rules and Regulations.

The Administrator has the discretionary power and authority to make such Plan Rules as the Administrator determines to be consistent with the terms, and necessary or advisable in connection with the administration, of the Plan and to modify or rescind any such Plan Rules.

8.3 Administrator's Discretion.

The Administrator has the discretionary power and authority to make all determinations necessary for administration of the Plan, except those determinations that the Plan requires others to make, and to construe, interpret, apply and enforce the provisions of the Plan and Plan Rules whenever necessary to carry out its intent and purpose and to facilitate its administration, including, without limitation, the discretionary power and authority to remedy ambiguities, inconsistencies, omissions and erroneous benefit calculations. In the exercise of its discretionary power and authority, the Administrator will treat all similarly situated persons uniformly.

8.4 Specialist's Assistance.

The Administrator may retain such actuarial, accounting, legal, clerical and other services as may reasonably be required in the administration of the Plan, and may pay reasonable compensation for such services. All costs of administering the Plan will be paid by the Participating Employers.

8.5 Indemnification.

The Participating Employers jointly and severally agree to indemnify and hold harmless, to the extent permitted by law, each director, officer, and employee of any Affiliates against any and all liabilities, losses, costs and expenses (including legal fees) of every kind and nature that may be imposed on, incurred by, or asserted against such person at any time by reason of such person's services in connection with the Plan, but only if such person did not act dishonestly or in bad faith or in willful violation of the law or regulations under which such liability, loss, cost or expense arises. The Participating Employers have the right, but not the obligation, to select counsel and control the defense and settlement of any action for which a person may be entitled to indemnification under this provision.

8.6 **<u>Benefit Claim Procedure</u>.**

(a) The Administrator will notify a Participant in writing, within 90 days of the Participant's written application for benefits, of the Participant's eligibility or noneligibility for benefits under the Plan. If the Administrator determines that a Participant is not eligible for benefits or full benefits, the notice will:

(1) state the specific reasons for the denial of any benefits;

(2) provide a specific reference to the provision of the Plan on which the denial is based;

(3) provide a description of any additional information or material necessary for the claimant to perfect the claim, and a description of why it is needed;

(4) state that the claimant will be provided, on request and free of charge, reasonable access to, and copies of, all documents, records, and other information relevant to the claim;

(5) state the claimant's right to bring a civil action under ERISA Section 502(a) following a continued denial of a claim after appeal review; and

(6) provide an explanation of the Plan's claims review procedure and other appropriate information as to the steps to be taken if the Participant wishes to have the claim reviewed. If the Administrator determines that there are special circumstances requiring additional time to make a decision, the Administrator will notify the Participant of the special circumstances and the date by which a decision is expected to be made, and may extend the time for up to an additional 90-day period.

(b) If a Participant is determined by the Administrator not to be eligible for benefits or if the Participant believes that he or she or she is entitled to greater or different benefits, the Participant will be provided the opportunity to have his or her claim reviewed by the Administrator by filing a petition for review with the Administrator within 60 days after the Participant receives the notice issued by the Administrator. The petition must state the specific reasons the Participant believes he or she or she is entitled to benefits or greater or different benefits. Within 60 days after the Administrator receives the petition, the Administrator will give the Participant (and his or her counsel, if any) an opportunity to present his or her position to the Administrator in writing, and the Participant (or his or her counsel) may review the pertinent documents, and the Administrator will notify the Participant of its decision in writing within such 60-day period, stating specifically the basis of the decision written in a manner calculated to be understood by the Participant and the specific provisions of the Plan on which the decision is based. If because of special circumstances requiring additional time to make a decision, the 60-day period is not sufficient, the decision may be deferred for up to another 60-day period at the election of the Administrator, but notice of this deferral must be given to the Participant.

(c) The same procedure applies to the Beneficiary of a deceased Participant.

(d) A claimant must exhaust the procedure described in this section before pursuing the claim in any other proceeding.

8.7 <u>Disputes</u>.

(a) In the case of a dispute between a Participant or his or her Beneficiary and a Participating Employer, the Administrator or other person relating to or arising from the Plan, the United States District Court for the District of Minnesota is a proper venue for any action initiated by or against the Participating Employer, Administrator or other person and such court will have personal jurisdiction over any Participant or Beneficiary named in the action.

(b) Regardless of where an action relating to or arising from the participation in the Plan by any Participant is pending, the law as stated and applied by the United States Court of Appeals for the Eighth Circuit or the United States District Court for the District of Minnesota will apply to and control all actions relating to the Plan brought against the Plan, a Participating Employer, the Administrator or any other person or against any such Participant or his or her Beneficiary.

ARTICLE 9.
MISCELLANEOUS

9.1 Withholding and Offsets.

The Participating Employers and the Trustee retain the right to withhold from any compensation, deferral and/or benefit payment pursuant to the Plan, any and all income, employment, excise and other tax as the Participating Employers or Trustee deems necessary and the Participating Employers may offset against amounts then payable to a Participant or Beneficiary under the Plan any amounts then owing to the Participating Employers by such Participant or Beneficiary.

9.2 Other Benefits.

Neither amounts deferred nor amounts paid pursuant to the Plan constitute salary or compensation for the purpose of computing benefits under any other benefit plan, practice, policy or procedure of a Participating Employer unless otherwise expressly provided thereunder.

9.3 No Warranties Regarding Tax Treatment.

The Participating Employers make no warranties regarding the tax treatment to any person of any deferrals or payments made pursuant to the Plan and each Participant will hold the Administrator and the Participating Employers and their officers, directors, employees, agents and advisors harmless from any liability resulting from any tax position taken in good faith in connection with the Plan.

9.4 No Rights to Continued Employment or Service Created.

Neither the establishment of nor participation in the Plan gives any individual the right to continued employment or service on the Company's board of directors or limits the right of the Participating Employer to discharge, transfer, demote, modify terms and conditions of employment or service on the Company's board of directors or otherwise deal with any individual without regard to the effect which such action might have on him or her with respect to the Plan.

9.5 Special Provisions.

Special provisions of the Plan applicable only to certain Participants may be set forth on an exhibit to the Plan adopted in the same manner as an amendment to the Plan. In the event of a conflict between the terms of the exhibit and the terms of the Plan, the exhibit controls. Except as otherwise expressly provided in the exhibit, the generally applicable terms of the Plan control all matters not covered by the exhibit.

9.6 Successors.

Except as otherwise expressly provided in the Plan, all obligations of the Participating Employers under the Plan are binding on any successor to the Participating Employer whether the existence of such successor is the result of a direct or indirect purchase, merger, consolidation or otherwise of all or substantially all of the business and/or assets of the Participating Employer.

SEPARATION AGREEMENT AND RELEASE

[<u>To be signed after Employee's last day of employment</u>]

This Separation Agreement and Release ("Agreement") is entered into between Cathy Hall ("Employee"), and Select Comfort Corporation, along with its subsidiaries, successors, assigns, affiliates, parent and predecessor companies, and its present owners, directors, officers, employees and stockholders (the "Company").

RECITALS

A. Employee's employment with the Company terminated effective October 10, 2008 (the "Separation Date").

B. The parties wish to enter into this Agreement to fully and finally resolve all matters between them as set forth herein.

AGREEMENT

In consideration of the above recitals and the promises set forth in this Agreement, the parties agree as follows:

1. <u>Employee's Claims</u>. "Employee's Claims" means all rights to be paid or given anything by the Company, including overtime pay, Paid Time Off, expense reimbursements, back pay, front pay, reinstatement, compensatory damages, liquidated damages, punitive damages, attorneys' fees, costs, or interest, based on any claims related to Employee's employment with the Company or the termination of that employment, for:

   a. alleged wrongful discharge, breach of contract, breach of a covenant of good faith and fair dealing, fraud or misrepresentation, defamation, infliction of emotional distress, assault, battery, invasion of privacy, interference with contractual or business relationships, violation of any the Company policy or practice, and any other claims arising under the common law of any state; or

   b. alleged unlawful discrimination, harassment, or retaliation, or other alleged unlawful practices arising under any federal, state, or local statute, ordinance, or regulation including, without limitation, claims under Title VII of the Civil Rights Act of 1964 ("Title VII"), the Americans with Disabilities Act ("ADA"), the Age Discrimination in Employment Act ("ADEA"), the Minnesota Human Rights Act ("MHRA"), 42 U.S.C. § 1981 ("Section 1981"), Minn. Stat. § 181.81, the South Carolina Human Affairs Law, the Utah Antidiscrimination Act, the Employee Retirement Income Security Act ("ERISA"), the Family and Medical Leave Act ("FMLA"), the Equal Pay Act, the Worker Adjustment and Retraining Notification Act ("WARN"), the Fair Credit Reporting Act, the Fair Labor Standards Act, the National Labor Relations Act, the Older Workers

Benefit Protection Act (“OWBPA”), whistleblower protection laws, and workers’ compensation non-interference or non-retaliation statutes such as Minn. Stat. § 176.82.

2. Severance Benefits. As a result of Employee’s separation from employment and in exchange for signing this Agreement and releasing Employee’s Claims, Employee will receive the following Severance Benefits from the Company:

a. Separation Pay. The Company will pay Employee a total of Three Hundred Fifty-six Thousand Six Hundred Forty-six Dollars ($356,646.00) which is approximately one times employee’s base salary as of the Separation Date, plus one times employee’s 2008 target bonus, plus a pro rata portion of employee’s 2008 target bonus less relocation incentive repayment (as agreed to per attached relocation addendum). The Separation Pay will be paid to Employee in a lump sum on the first regular payroll date after expiration of the Rescission Period, which is defined below. Separation payments made under this Agreement shall be treated as taxable income, and subject to withholdings to the extent required by law.

b. Benefits Continuation. Except as otherwise provided below, for twelve (12) months following the Separation Date, if Employee elects to continue coverage under the Company’s group medical or dental plan for Employee and Employee’s dependents under COBRA, and if Employee timely executes all documents necessary to make such election, the Company will reimburse Employee an amount equal to the difference between the amount Employee pays for such continued coverage each week and the amount paid by an active, full-time employee in each such week for the same level of coverage elected by Employee. The Company’s obligations under this paragraph shall immediately cease, however, on (i) the date on which Employee’s eligibility for COBRA continuation coverage ends or (ii) the date on which Employee becomes eligible to participate in another group medical plan, due to reemployment or otherwise, whether or not Employee elects to participate in such plan and whether or not such plan provides comparable benefits or includes limitations or exclusions (unless such other group medical plan contains a pre-existing condition exclusion that affects the Employee’s coverage under such plan). Further, the Company’s obligations under this paragraph are subject to Employee providing, to the satisfaction of the Company, proof of COBRA election and proof of payment of premiums by Employee.

c. Outplacement Assistance. The Company will assist Employee in Employee’s career transition by paying for up to twelve (12) months of outplacement services from a consultant to be selected by the Company. Such payments will be made directly to the consultant by the Company.

Employee agrees that the benefits described above constitute sufficient compensation for all of Employee’s promises contained in this Agreement, including

Employee's Release of Claims set forth below. Employee understands that Employee will not receive any of the Severance Benefits described above if Employee exercises the right of rescission described below.

3. Release of Employee's Claims. Employee agrees that the Severance Benefits Employee will receive are in addition to anything of value that Employee would be entitled to receive from the Company if Employee did not sign this Agreement. In exchange for the Severance Benefits, and by signing this Agreement, Employee agrees to waive all of Employee's Claims. Employee will not bring any lawsuits against the Company, or make any demands against the Company for compensation or damages, based on Employee's Claims. The Severance Benefits Employee is receiving in exchange for signing this Agreement are fair payment for the release of Employee's Claims. However, Employee's release does not include, and Employee is not waiving, any Claims that the law does not allow to be waived, or any claims that may arise after the date on which Employee signs this Agreement.

Employee's release does not limit Employee's right to file a charge under Title VII, ADEA, ADA, Section 1981 or any other civil rights statute, regulation, or ordinance, or Employee's right to participate in an investigation or proceeding conducted by the EEOC or other Federal, state or local anti-discrimination agency. However, Employee agrees that if Employee signs this Agreement and such a charge or a lawsuit is brought in Employee's name before any such government agency, Employee will not be able to recover money or other damages for any of Employee's Claims.

4. Paid Time Off. Regardless of whether Employee signs this Agreement, the Company will pay Employee for all Paid Time Off ("PTO") that Employee has earned but not used as of the Separation Date.

5. No Other Benefits. Employee understands that except for those items of compensation and benefits specifically described in this Agreement, after the Separation Date, Employee shall receive no other benefits and shall no longer participate in any of the Company's benefit plans, except as required under state and federal benefit continuation laws. All of Employee's rights under such plans shall be governed by the terms of such plans.

6. Restrictions.

a. Confidentiality. Employee agrees that this Agreement and all of its terms shall remain completely confidential, and that Employee will not share them with anyone, either before or after Employee signs this Agreement, except that Employee may reveal the terms of this Agreement to Employee's accountants or other financial advisors, legal counsel, and spouse or domestic partner, if these individuals agree to be bound by the terms of this provision, to appropriate governmental agencies, and as required by law.

b. Nondisparagement. Employee agrees that Employee will not, directly or indirectly, at any time, make any defaming or disparaging remark, either oral or in writing, regarding the Company, its products or services, or any of its employees, officers, directors, affiliates or agents, either individually or in any representative capacity. Employee further agrees not to foment, encourage, incite or assist any claims, complaints or protests of any kind by any third party against the Company or any of its employees, officers, directors, affiliates or agents. In the event that Employee receives a subpoena from a party other than the Company, Employee shall promptly notify the Company and provide it with a copy of the subpoena so that the Company has an opportunity to seek to quash or otherwise respond to the subpoena.

c. Damages for Violation of Confidentiality and Nondisparagement Provisions. Employee acknowledges and agrees that the Confidentiality and Nondisparagement provisions of this Agreement are significant inducements for the Company to enter into this Agreement, and that any violation of either of these provisions by Employee would irreparably harm the Company in ways that cannot be measured. In the event of any such violation, the Company shall be entitled to bring a legal action for appropriate equitable relief as well as damages, including recovery of its reasonable attorneys' fees and costs from Employee.

d. Cooperation in Transition. Employee agrees to continue to devote Employee's best efforts to the performance of Employee's duties and to assist the Company in transitioning Employee's work to other employees. If the Company believes, it its discretion, that Employee is not complying with this paragraph, the Company has the right to revoke the offer set forth in this Agreement and Employee will not be entitled to the Severance Benefits.

7. Opportunity to Consider and Seek Advice. Employee has been advised by the Company to consult with an attorney prior to signing this Agreement. Employee further understands that Employee has twenty-one (21) days from the date on which Employee receives this Agreement, not counting the day on which Employee receives it, to consider whether or not to sign it ("Consideration Period"). Employee may sign this Agreement earlier if Employee wishes; provided, however, that Employee may not sign this Agreement prior to the Separation Date. Employee agrees that if Employee signs this Agreement before the end of the Consideration Period, it will be Employee's voluntary decision to do so because Employee decided Employee did not need additional time to decide whether to sign this Agreement.

8. Opportunity to Rescind. Employee understands that he may rescind or cancel this Agreement within fifteen (15) days after the date on which he signs it, not counting the day upon which he signs it ("Rescission Period"). This Agreement will not become effective or enforceable unless and until the 15-day Rescission Period has expired without Employee revoking the Agreement.

9. Procedure for Accepting or Revoking the Agreement. To accept the terms of this Agreement, Employee must deliver it, after signing and dating it, to the Company by hand or by mail within the Consideration Period. To rescind the release of Employee's Claims, Employee must deliver a written, signed statement that Employee revokes or cancels Employee's acceptance to the Company by hand or by mail within the 15-day Rescission Period. All deliveries must be made to the Company at the following address:

Lisa Eull
Director, Benefits
Select Comfort Corporation
9800 59th Avenue North
Minneapolis, MN 55442

If Employee chooses to deliver Employee's acceptance of this Agreement or rescission of the release of Employee's Claims by mail, it must be:

a. postmarked within the period stated above;

b. properly addressed to the Company at the address stated above; and

c. sent by certified mail.

10. Return of Property. Employee certifies that Employee has returned the originals and all copies of all Company files, documents, software, hardware, keys, credit cards, office equipment, and all other property of the Company in Employee's possession or under Employee's control. If Employee finds any Company property after Employee signs this Agreement, Employee agrees to return the property to the Company promptly.

11. Non-Admission. The Company denies that it has violated any legal obligation or engaged in any wrongdoing, and nothing in this Agreement is intended to be, nor will be deemed to be, an admission of liability by the Company or a waiver of any defense.

12. Entire Agreement. Except for the Employee Inventions, Confidentiality and Non-compete Agreement signed on November 1, 2007 (copy enclosed), this Agreement contains the entire agreement between the parties and replaces any and all oral and written agreements and communications between the parties regarding the subject matter addressed in this Agreement. Employee acknowledges that Employee has not relied upon any representation or statement made by the Company or by any of the Company's agents, attorneys or representatives with regard to the subject matter, scope or effect of this Agreement or otherwise, other than those specifically stated in this Agreement.

13. Invalidity. In case any one or more of the provisions of this Agreement is held to be invalid, illegal or unenforceable in any respect, the validity, legality and

enforceability of the remaining provisions of this Agreement will not in any way be affected or impaired.

14. Voluntary and Knowing Action. Employee acknowledges that Employee has had the opportunity to consult with counsel of Employee's choosing, has read and understood the terms of this Agreement, and is voluntarily entering into this Agreement to resolve all of Employee's Claims.

15. Governing Law. Employee understands that Minnesota law governs this Agreement. Employee agrees that any dispute relating to this Agreement will be subject to the jurisdiction of the state and federal courts located within the State of Minnesota, Hennepin County, and that venue there is proper.

16. Binding and Enforceable Agreement. The Parties acknowledge that they have entered into this Agreement intending it to be legally binding and enforceable.

Dated: October 22, 2008

/s/ Cathy Hall

Cathy Hall

Dated: October 24, 2008

SELECT COMFORT CORPORATION

/s/ Scott Peterson

By: Scott Peterson

Its: Senior Vice President, Human Resources

Exhibit 10.34

**FIRST AMENDMENT TO THE
AMENDED AND RESTATED
SELECT COMFORT CORPORATION
EXECUTIVE SEVERANCE PAY PLAN**

Pursuant to the retained power of amendment contained in Section 6.1 of the "Select Comfort Corporation Executive Severance Pay Plan," as previously amended and restated as of August 21, 2008 (the "Plan"), the undersigned amends the Plan as set forth below.

Section 4.4(A) of the Plan is amended, effective December 12, 2008 (and applies to any Qualified Employee who has a Termination of Employment after that date) to read as follows:

(A)

(1) With respect to a Qualified Employee who is classified by the Participating Employer as a Grade 14 or 15, the base amount of Severance Pay benefits pursuant to Section 4.1 will be paid in a single lump sum within a reasonable time following the Participant's Termination of Employment (subject to the provisions of Section 3.3 relating to execution and delivery of a Release within the period prescribed by the Administrator and no rescission of any such Release) and in no event later than March 1st of the calendar year following the calendar year during which such Termination of Employment occurs.

(2) With respect to a Qualified Employee who is classified by the Participating Employer as a Grade 13, the base amount of Severance Pay benefits pursuant to Section 4.1 will be paid in substantially equal installments at regular payroll intervals beginning not more than forty-five (45) days after the Participant's Termination of Employment (subject to the provisions of Section 3.3 relating to execution and delivery of a Release within the period prescribed by the Administrator and no rescission of any such Release); provided, that any portion of the base amount of Severance Pay benefits pursuant to Section 4.1 that would exceed the limitations of the separation pay exception to Code section 409A (as described in Treasury Regulation section 1.409A-1(b)(9)) will be paid in a single lump sum within a reasonable time following the Participant's Termination of Employment (subject to the provisions of Section 3.3 relating to execution and delivery of a Release within the period prescribed by the Administrator and no rescission of any such Release) and in no event later than March 1st of the calendar year following the calendar year during which such Termination of Employment occurs.

(3) Severance Pay benefits paid in installments at regular payroll intervals are intended to comply with the separation pay exception to Code section 409A (as described in Treasury Regulation section 1.409A-1(b)(9)). Severance Pay benefits paid in a single lump sum payment are intended to comply with the short-term deferral exception to Code section 409A (as described in Treasury Regulations section 1.409A-1(b)(4)) because such benefits will be paid not later than March 15th of the calendar year following the calendar year in

which the employee’s right to the benefits is no longer subject to a substantial risk of forfeiture within the meaning of Code section 409A

IN WITNESS WHEREOF, the Company has caused this instrument to be executed by its authorized officers on the date written below.

	SELECT COMFORT CORPORATION
Dated: December 12, 2008	By: /s/ Mark A. Kimball Senior Vice President & General Counsel
Dated: December 12, 2008	By: /s/ Karen R. Richard Vice President, Chief Human Resource and Strategy Officer

Exhibit 21.1

SUBSIDIARIES OF SELECT COMFORT CORPORATION

Name of Subsidiary	Organized under the Laws of
Select Comfort Retail Corporation	Minnesota (USA)
Select Comfort Canada Holding Inc.	Minnesota (USA)
selectcomfort.com corporation	Minnesota (USA)
Select Comfort COSC Canada ULC	Alberta, Canada
Select Comfort Limited	United Kingdom

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

The Board of Directors
Select Comfort Corporation:

We consent to the incorporation by reference in the registration statements (No. 333-70493, No. 333-79157, No. 333-74876, No. 333-84329, No. 333-80755, No. 333-85914 and No. 333-118329) on Form S-8 of Select Comfort Corporation and subsidiaries of our reports dated March 19, 2009, with respect to the consolidated balance sheets of Select Comfort Corporation and subsidiaries as of January 3, 2009 and December 29, 2007, and the related consolidated statements of operations, shareholders' (deficit) equity, and cash flows for each of the fiscal years in the three-year period ended January 3, 2009, and the related financial statement schedule, and the effectiveness of internal control over financial reporting as of January 3, 2009, which reports appear in the January 3, 2009 annual report on Form 10-K of Select Comfort Corporation.

Our report dated March 19, 2009 contains an explanatory paragraph that states that the Company's losses from operations and inability to generate sufficient cash flow to meet obligations and sustain operations raises substantial doubt about its ability to continue as a going concern. The consolidated financial statements and financial statement schedule do not include any adjustments that might result from the outcome of this uncertainty. Our report also refers to the adoption of the provisions of SFAS 157, *Fair Value Measurements*, and SFAS 159, *The Fair Value Option for Financial Assets and Liabilities*, on December 30, 2007 and FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, on December 31, 2006.

KPMG LLP

Minneapolis, Minnesota
March 19, 2009

Exhibit 31.1

Certification by Chief Executive Officer

I, William R. McLaughlin, certify that:

1. I have reviewed this annual report on Form 10-K 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c) 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

    d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant's other certifying officer 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: March 19, 2009

/s/ William R. McLaughlin
William R. McLaughlin
Chief Executive Officer

Exhibit 31.2

Certification by Chief Financial Officer

I, James C. Raabe, certify that:

1. I have reviewed this annual report on Form 10-K 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c) 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

    d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant's other certifying officer 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: March 19, 2009

/s/ James C. Raabe
James C. Raabe
Senior Vice President and Chief Financial Officer

Exhibit 32.1

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

In connection with the Annual Report of Select Comfort Corporation (the "Company") on Form 10-K for the fiscal year ended January 3, 2009, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, William R. McLaughlin, Chief Executive Officer of the Company, solely for the purposes of 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, does hereby certify, to his knowledge, 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.

Date: March 19, 2009

/s/ William R. McLaughlin
William R. McLaughlin
Chief Executive Officer

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. §1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Select Comfort Corporation (the "Company") on Form 10-K for the fiscal year ended January 3, 2009, 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. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, does hereby certify, to his knowledge, 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.

Date: March 19, 2009

/s/ James C. Raabe
James C. Raabe
Senior Vice President and Chief Financial Officer

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.