

Note: This form was not filed with the
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

QUARTERLY REPORT PURSUANT TO THE INDENTURE, DATED AS OF OCTOBER 4, 2005 AMONG BROOKSTONE, INC., A DELAWARE CORPORATION, BROOKSTONE COMPANY, INC., THE GUARANTORS (AS DEFINED THEREIN) AND WELLS FARGO BANK, N.A., AS TRUSTEE

For the quarterly period ended
July 4, 2009

BROOKSTONE, INC.

(Exact name of company as specified in its charter)

| | | |
|---|---|--|
| Delaware (State of Incorporation) | One Innovation Way Merrimack, NH 03054 (Address of Principal Executive Offices) | 06-1182895 (I.R.S. Employer Identification No.) |
|---|---|--|

603-880-9500
(Company's Telephone Number, Including Area Code)

Indicate by check mark whether the company (1) has filed with the Securities Exchange Commission or posted on its website all reports required to be prepared pursuant to the Indenture, dated as of October 4, 2005, among the Company, Brookstone Company, Inc., each of the Guarantors and Wells Fargo Bank, N.A. as Trustee during the preceding 12 months (or for such shorter period that the company was required to prepare such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the company 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. (Check one):

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

Indicate by check mark whether the company is a shell company (as defined in Rule 12b-2 of the Act) Yes No

The company had one share of common stock, par value \$0.01, outstanding as of August 13, 2009.

Brookstone, Inc.
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PART I - FINANCIAL INFORMATION

ITEM 1. *Financial Statements*

BROOKSTONE, INC. CONSOLIDATED BALANCE SHEETS (In thousands, except share data)

| | July 4, 2009 (Unaudited) | January 3, 2009 | June 28, 2008 (Unaudited) |
|--|-----------------------------|-------------------|------------------------------|
| <u>Assets</u> | | | |
| Current assets: | | | |
| Cash and cash equivalents | \$ 2,024 | \$ 22,530 | \$ 1,566 |
| Receivables, net | 6,628 | 9,839 | 8,683 |
| Merchandise inventories | 66,242 | 82,095 | 92,122 |
| Deferred income taxes, net | --- | --- | 16,802 |
| Prepaid expenses | 2,583 | 16,379 | 11,071 |
| Total current assets | 77,477 | 130,843 | 130,244 |
| Property, plant and equipment, net | 61,755 | 66,456 | 70,363 |
| Intangible assets, net | 105,000 | 105,000 | 129,167 |
| Goodwill | 99,734 | 99,734 | 189,524 |
| Other assets | 7,090 | 8,565 | 10,257 |
| Total assets | <u>\$ 351,056</u> | <u>\$ 410,598</u> | <u>\$ 529,555</u> |
| <u>Liabilities and Shareholder's Equity</u> | | | |
| Current liabilities: | | | |
| Accounts payable | \$ 10,483 | \$ 17,033 | \$ 14,947 |
| Other current liabilities | 25,709 | 41,179 | 29,983 |
| Short-term borrowings | 7,000 | --- | --- |
| Total current liabilities | 43,192 | 58,212 | 44,930 |
| Other long-term liabilities | 21,474 | 21,370 | 19,934 |
| Long-term debt, net of current portion | 173,779 | 174,089 | 174,466 |
| Deferred income taxes | 38,020 | 38,430 | 43,052 |
| Total liabilities | 276,465 | 292,101 | 282,382 |
| Commitments and contingencies (See Note 6) | --- | --- | --- |
| Equity: | | | |
| Brookstone Shareholder's equity: | | | |
| Common Stock – \$0.01 par value, 1,000 shares authorized, one share issued and outstanding | --- | --- | --- |
| Additional paid-in capital | 241,546 | 241,205 | 240,797 |
| Accumulated other comprehensive income (loss) | (542) | (532) | 575 |
| Retained earnings (deficit) | (167,305) | (123,216) | 4,693 |
| Total Brookstone Shareholder's equity | 73,699 | 117,457 | 246,065 |
| Noncontrolling interests | 892 | 1,040 | 1,108 |
| Total equity | 74,591 | 118,497 | 247,173 |
| Total liabilities and equity | <u>\$ 351,056</u> | <u>\$ 410,598</u> | <u>\$ 529,555</u> |

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

BROOKSTONE, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands)
(Unaudited)

| | Thirteen weeks ended | | Twenty-six weeks ended | |
|---|-----------------------------|----------------------|-------------------------------|----------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Net sales | \$ 72,972 | \$ 97,390 | \$ 134,431 | \$ 187,191 |
| Cost of sales | <u>58,387</u> | <u>70,876</u> | <u>113,278</u> | <u>138,892</u> |
| Gross profit | 14,585 | 26,514 | 21,153 | 48,299 |
| Selling, general and administrative expenses | <u>25,069</u> | <u>34,232</u> | <u>52,421</u> | <u>68,967</u> |
| Loss from operations | (10,484) | (7,718) | (31,268) | (20,668) |
| Interest expense, net | <u>5,995</u> | <u>5,902</u> | <u>11,975</u> | <u>11,524</u> |
| Loss before income taxes | (16,479) | (13,620) | (43,243) | (32,192) |
| Income tax provision (benefit) | <u>91</u> | <u>(5,328)</u> | <u>564</u> | <u>(12,435)</u> |
| Consolidated net loss | (16,570) | (8,292) | (43,807) | (19,757) |
| Less: Net income attributable to noncontrolling interests | <u>169</u> | <u>370</u> | <u>282</u> | <u>636</u> |
| Net loss attributable to Brookstone | <u>\$ (16,739)</u> | <u>\$ (8,662)</u> | <u>\$ (44,089)</u> | <u>\$ (20,393)</u> |

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

BROOKSTONE, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

| | Twenty-six weeks ended | |
|---|-------------------------------|----------------------|
| | July 4, 2009 | June 28, 2008 |
| Cash flows from operating activities: | | |
| Consolidated net loss | \$ (43,807) | \$ (19,757) |
| Adjustments to reconcile consolidated net loss to net cash used for operating activities: | | |
| Depreciation and amortization | 7,249 | 7,685 |
| Amortization of debt issuance costs | 1,069 | 1,068 |
| Amortization of debt discount | 141 | 141 |
| Amortization of revaluation of leases | (76) | (29) |
| Loss on disposal of property, plant and equipment | 139 | 572 |
| Share-based compensation expense | 341 | (214) |
| Deferred income taxes, net | (410) | (12,572) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable, net | 3,181 | 4,267 |
| Merchandise inventories | 15,853 | 14,278 |
| Prepaid expenses | 13,796 | (7,051) |
| Other assets | 112 | 119 |
| Accounts payable | (6,550) | (18,560) |
| Other current liabilities | (15,470) | (31,231) |
| Other long-term liabilities | 464 | (182) |
| Net cash used for operating activities | (23,968) | (61,466) |
| Cash flows from investing activities: | | |
| Expenditures for property, plant and equipment, net | (2,687) | (6,461) |
| Net cash used for investing activities | (2,687) | (6,461) |
| Cash flows from financing activities: | | |
| Borrowings from senior secured credit facility, net | 7,000 | --- |
| Payments on long-term debt and capital lease | (451) | (452) |
| Capital contributions by noncontrolling interests | 48 | 253 |
| Cash distributions to noncontrolling interests | (448) | (1,165) |
| Net cash provided by (used for) financing activities | 6,149 | (1,364) |
| Net decrease in cash and cash equivalents | (20,506) | (69,291) |
| Cash and cash equivalents at beginning of period | 22,530 | 70,857 |
| Cash and cash equivalents at end of period | \$ 2,024 | \$ 1,566 |

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

BROOKSTONE, INC.

Notes to Consolidated Financial Statements

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared by Brookstone, Inc. (“we”, “our” “us” or “the Company”) in accordance with accounting principles generally accepted in the United States of America, which require us to make judgments, estimates and assumptions that affect the results of operations, financial position and cash flows, as well as the related footnote disclosures. We evaluate our estimates on an on-going basis using our historical experience as well as other factors we believe are appropriate under the circumstances, such as current economic conditions, and adjust or revise our estimates as circumstances change. As future events and their effect cannot be determined with precision, actual results may differ from these estimates. In the opinion of Brookstone, Inc., these financial statements contain all adjustments (consisting of only normal recurring adjustments, except as specifically disclosed) necessary to present fairly the financial position, the results of operations, and the cash flows for the periods reported. Certain information and footnote disclosures normally included in annual financial statements presented in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted, for purposes of the interim financial statements. The accompanying unaudited consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto for the Fiscal year ended January 3, 2009, which may be found in the Company’s Fiscal 2008 annual report on Form 10-K, as posted on the Company’s website at www.brookstone.com.

The results of the thirteen and twenty-six week periods ended July 4, 2009 are not necessarily indicative of the results for the full fiscal year. The Company’s business, like the business of retailers in general, is subject to seasonal influences and fluctuations. Historically, the Company’s fourth fiscal quarter, which includes the winter holiday selling season, has produced a disproportionate amount of the Company’s net sales and substantially all of its income from operations. The Company expects that its business will continue to be subject to such seasonal influences.

Brookstone, Inc. is a privately held, indirect wholly-owned subsidiary of OSIM Brookstone Holdings, L.P. (“OBH L.P.”), the general partner of which is OSIM Brookstone Holdings, Inc. (“OBH GP”).

2. Recent Accounting Pronouncements

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 168, *The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles a Replacement of FASB Statement No. 162*. This Standard establishes the FASB Accounting Standards Codification™ (the “Codification”) as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. GAAP. The Codification does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all the authoritative literature related to a particular topic in one place. The Codification is effective for interim and annual periods ending after September 15, 2009, and as of the effective date, all existing accounting standard documents will be superseded. The Codification is effective for our Company in the third quarter of 2009, and accordingly, our Quarterly Report on Form 10-Q for the quarter ending October 3, 2009 and all subsequent financial statements will reference the Codification as the sole source of authoritative literature.

In June 2009, the FASB issued SFAS No. 167, *Amendments to FASB Interpretation No. 46(R)*, which modifies how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. SFAS 167 clarifies that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity’s purpose and design and a company’s ability to direct the activities of the entity that most significantly impact the entity’s economic performance. SFAS 167 requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity. SFAS 167 also requires additional disclosures about a company’s involvement in variable interest entities and any significant changes in risk exposure due to that involvement. SFAS 167 is

effective for fiscal years beginning after November 15, 2009. We have not completed our assessment of the impact SFAS 167 will have on our consolidated financial statements.

In June 2009, the FASB issued SFAS No. 166, *Accounting for Transfers of Financial Assets — an amendment of FASB Statement No. 140*, which requires entities to provide more information regarding sales of securitized financial assets and similar transactions, particularly if the entity has continuing exposure to the risks related to transferred financial assets. SFAS 166 eliminates the concept of a “qualifying special-purpose entity,” changes the requirements for derecognizing financial assets and requires additional disclosures. SFAS 166 is effective for fiscal years beginning after November 15, 2009. We have not completed our assessment of the impact SFAS 166 will have on our consolidated financial statements, if any.

In May 2009, the FASB issued SFAS No. 165, *Subsequent Events*, which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. SFAS 165 also requires entities to disclose the date through which subsequent events were evaluated as well as the rationale for why that date was selected. SFAS 165 is effective for interim and annual periods ending after June 15, 2009, and accordingly, we adopted this Standard during the second quarter of 2009. SFAS 165 requires that public entities evaluate subsequent events through the date that the financial statements are issued. We have evaluated subsequent events through the time of the posting of these financial statements to our website at www.brookstone.com on August 14, 2009.

In April 2009, the FASB issued FASB Staff Position (FSP) FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*. This FSP requires disclosures about the fair value of financial instruments whenever a public company issues financial information for interim reporting periods. This FSP was effective for our Company on April 5, 2009. The adoption of FSP FAS 107-1 and APB 28-1 did not have a significant impact to our consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133*. SFAS No. 161 applies to all derivative instruments and related hedged items accounted for under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS No. 133). SFAS No. 161 requires entities to provide greater transparency about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity’s financial position, results of operations and cash flows. SFAS No. 161 was effective for our Company on January 4, 2009. The adoption of SFAS No. 161 did not have a significant impact to our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements — an amendment of Accounting Research Bulletin No. 51*. SFAS No. 160 establishes accounting and reporting standards for noncontrolling interests (previously referred to as minority interests) in subsidiaries. SFAS No. 160 requires that a noncontrolling interest in a subsidiary should be accounted for as a component of equity separate from the parent’s equity, rather than as a liability. SFAS No. 160 was effective for our Company on January 4, 2009, and is being applied prospectively, except for the presentation and disclosure requirements, which have been applied retrospectively. The adoption of SFAS No. 160 altered the presentation of noncontrolling interests in our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations*. SFAS No. 141(R) amends the principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree and the goodwill acquired. SFAS No. 141(R) also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. SFAS No. 141(R) was effective for our Company on January 4, 2009, and the Company will apply SFAS No. 141(R) prospectively to all business combinations subsequent to the effective date. The adoption of SFAS No. 141(R) did not have a significant impact on our consolidated financial statements, and the impact that its adoption will have on our consolidated financial statements in future periods will depend on the nature and size of business combinations completed subsequent to the date of adoption.

3. Comprehensive Loss

Comprehensive loss consists of net loss attributable to Brookstone and amortization of certain pension and post-retirement liability adjustments. Total comprehensive loss for the thirteen and twenty-six week periods ended July 4, 2009 and June 28, 2008 is presented below (in thousands):

| | Thirteen weeks ended | | Twenty-six weeks ended | |
|---|----------------------|-------------------|------------------------|--------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Net loss attributable to Brookstone | \$ (16,739) | \$ (8,662) | \$ (44,089) | \$ (20,393) |
| Other comprehensive loss: | | | | |
| Amortization of certain pension /post-retirement liability adjustments (net of tax of \$0, \$(5), \$0 and \$(11), respectively) | (5) | (9) | (10) | (18) |
| Total comprehensive loss | <u>\$ (16,744)</u> | <u>\$ (8,671)</u> | <u>\$ (44,099)</u> | <u>\$ (20,411)</u> |

4. Shareholder's Equity

Share-Based Compensation

The Company accounts for share-based awards under SFAS No. 123(R), which requires measurement of compensation cost for all share-based awards at fair value on date of grant and recognition of compensation over the service period for awards expected to vest.

Certain members of the Company's management hold Class B limited partnership interests in OBH LP ("Class B" Interests). These interests are restricted awards that vest either ratably over five years or require certain financial returns be met. Management has determined that these awards should be accounted for under push down accounting. The fair value of restricted awards granted, are estimated at the date of grant using a Black-Scholes option-pricing model. There were no grants of restricted awards during the twenty-six weeks ended July 4, 2009 or June 28, 2008.

The Company recognizes compensation expense, net of an estimated forfeiture rate, on a straight-line basis over the requisite service period of the award. The estimated forfeiture rate was based on historical experience. Under the provisions of SFAS No. 123(R), expense is recognized only for those awards expected to fully vest. If actual forfeitures differ from the estimates, a revision to the forfeiture rate will be necessary.

The Company recognized compensation expense of \$152 thousand and \$341 thousand for the thirteen and twenty-six week periods ending July 4, 2009 and \$209 thousand and \$418 thousand for the thirteen and twenty-six week periods ending June 28, 2008, respectively, related to the Class B Interests, which are classified in Selling, General and Administrative expenses. There was no related income tax effect. At July 4, 2009, the Company had approximately \$1.9 million of Class B Interests remaining to be expensed over the period through May 2012.

Under the terms of his succession agreement, a former Chief Executive Officer of the Company retains a "Put Right", whereby he has the right to require OBH LP to pay him, in exchange for him relinquishing his Class A limited partnership interests of OBH LP, a "Put Price" determined as provided therein during the thirty (30) day period following April 18, 2011. As of June 28, 2008, the Company recorded an "other long-term liability" of approximately \$672 thousand, in conjunction with this Put Right. This Put Right had a zero value at July 4, 2009 and January 3, 2008. Accordingly, there was no compensation expense related to this Put Right for the thirteen or twenty-six week periods ended July 4, 2009, while the decrease in the Put Right value resulted in a reversal of previously recognized compensation expense of approximately \$467 thousand and \$632 thousand for the thirteen and twenty-six week periods ending June 28, 2008, respectively, which is classified in Selling, General and Administrative expenses.

5. Fair Value Measurements

Effective December 30, 2007 for financial assets and liabilities and January 4, 2009 for non-financial assets and liabilities, the Company adopted SFAS No. 157, which defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. The financial assets and liabilities measured at fair value on a recurring basis are limited to the Company's interest rate swap instrument (refer to Note 10 for further discussion). The Company's non-financial assets and liabilities that are measured at fair value include any long-lived assets that are impaired in a current reported period. There were no such assets or liabilities in the current period.

SFAS No. 157 establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The following table presents the fair value and the hierarchy levels, for financial assets and liabilities that are measured at fair value on a recurring basis as of July 4, 2009 (in thousands):

| | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|----------------------------------|----------------|----------------|----------------|
| Assets | \$ - | \$ - | \$ - |
| Liabilities: | | | |
| Derivative financial instruments | \$ - | \$ 135 | \$ - |

Derivative financial instruments consist of an interest rate swap for which fair value is determined through the use of a pricing model, which utilizes verifiable inputs such as market interest rates which are observable at commonly quoted intervals for the full term of the swap agreement.

The recorded amounts for cash and cash equivalents, other current assets, accounts receivable, accounts payable and other current liabilities approximate fair value due to the short-term nature of these assets and liabilities and long term debt related to the Company's capital lease on its distribution center and the real estate loan on its Headquarters facility approximates fair value due to variable interest rates. At July 4, 2009, the carrying amount of long-term debt of the 12% Second Lien Senior Secured Notes was \$169.1 million, which is net of an unamortized debt discount of \$0.9 million. The estimated fair value at July 4, 2009 was \$74.8 million, based on quoted market prices for such notes.

6. Contingencies

Legal Proceedings

Alvarez, et al. v. Brookstone Co., Inc.

As previously reported in our Annual Report on Form 10-K for fiscal year 2008, on December 10, 2008, a putative class action was commenced against us in California Superior Court for San Diego County. The complaint and subsequently filed amended complaint alleged, among other things, that we violated the California Credit Card Act of 1971 by requesting that customers using credit cards provide "personal

identification information" in the form of zip codes. The Plaintiff also alleged an invasion of the right to privacy protected by the California Constitution. In addition to statutory and other unspecified damages, the lawsuit sought injunctive relief and an award of attorneys' fees. On July 27, 2009, the Court sustained our demurrer to all of the claims in the amended complaint without leave to amend. We do not know whether the Plaintiff will seek to appeal this ruling.

As of July 4, 2009, the end of the quarterly period covered by this report, we were subject to the various legal proceedings and claims discussed above, as well as certain other legal proceedings and claims that have not been fully resolved and that have arisen in the ordinary course of business. In the opinion of management, we do not have a potential liability related to any current legal proceedings and claims that would individually or in the aggregate have a material adverse effect on its financial condition or operating results. However, the results of legal proceedings cannot be predicted with certainty. Should we fail to prevail in any of these legal matters or should several of these legal matters be resolved against us in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

7. Segment Information

The Company operates in two reportable segments based on its two distinct distribution channels; retail and direct marketing. The retail segment is comprised of all full-year stores in addition to all temporary stores and kiosks. Retail product distribution is conducted primarily through the store locations. The direct marketing segment is comprised of the *Brookstone* catalog and products promoted via our internet website, www.brookstone.com and sales to corporate and wholesale customers. Direct marketing product distribution is primarily conducted through the Company's direct marketing customer sales and contact center and distribution center located in Mexico, Missouri and by its vendors. Both segments of the Company sell similar products, although not all Company products are available through both segments.

All costs directly attributable to the direct marketing segment are charged to this segment while all remaining operating costs are charged to the retail segment. The Company's management does not review assets by segment, and it is impracticable for the Company to report revenues by product or to group similar products.

The tables below disclose segment net sales and income (loss) before taxes for the thirteen and twenty-six week periods ended July 4, 2009 and June 28, 2008 (in thousands).

Thirteen weeks ended:

| | Net Sales | | Income (Loss) Before Taxes | |
|--------------------------|------------------|------------------|----------------------------|--------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Reportable segment: | | | | |
| Retail | \$ 61,142 | \$ 77,314 | \$ (12,002) | \$ (9,781) |
| Direct Marketing | 11,830 | 20,076 | 1,349 | 1,693 |
| Reconciling items: | | | | |
| Interest expense | --- | --- | (5,998) | (6,014) |
| Interest income | --- | --- | 3 | 112 |
| Noncontrolling interests | --- | --- | 169 | 370 |
| Consolidated: | <u>\$ 72,972</u> | <u>\$ 97,390</u> | <u>\$ (16,479)</u> | <u>\$ (13,620)</u> |

Twenty-six weeks ended:

| | Net Sales | | Income (Loss) Before Taxes | |
|--------------------------|-------------------|-------------------|----------------------------|--------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Reportable segment: | | | | |
| Retail | \$ 112,526 | \$ 150,329 | \$ (32,702) | \$ (23,099) |
| Direct Marketing | 21,905 | 36,862 | 1,152 | 1,795 |
| Reconciling items: | | | | |
| Interest expense | --- | --- | (11,981) | (12,077) |
| Interest income | --- | --- | 6 | 553 |
| Noncontrolling interests | --- | --- | 282 | 636 |
| Consolidated: | <u>\$ 134,431</u> | <u>\$ 187,191</u> | <u>\$ (43,243)</u> | <u>\$ (32,192)</u> |

8. Joint Ventures and Variable Interest Entity

The Company enters into various joint venture arrangements to operate certain airport stores under separate agreements with respect to each city. As of July 4, 2009, the Company operated 11 airport store locations through seven separate joint venture agreements. All joint ventures have been consolidated since inception based on the Company's majority ownership interest and voting rights, with the exception of the Atlanta venture as discussed below.

Under the requirements of FASB Interpretation No. ("FIN") 46(R), *Consolidation of Variable Interest Entities-an Interpretation of ARB No. 51*, ("FIN 46(R)") as amended, variable interest entities are required to be consolidated if the total equity investment at risk is not sufficient to permit the entity to finance its activities without financial support or the equity investors lack certain specified characteristics of a controlling financial interest. While the Company has only a 49% ownership interest in the Atlanta venture, our voting rights represent 50% of the total voting rights based on the structure of the venture. This "disproportionate" relationship of ownership interests to the voting rights and the inability to unilaterally make decisions (without approval from the other party) are primary factors in determining the lack of a controlling financial interest, under FIN 46(R). As a result, the Company determined that the Atlanta joint venture qualifies as a Variable Interest Entity ("VIE"). Under FIN 46(R), an enterprise with a variable interest shall treat variable interests in that same entity held by its related parties as its own interests. The other party in the Atlanta venture qualifies as a related party since the other party received its interest in the venture through a loan from the venture. The party within this "related party group" that is most closely associated with the variable interest entity is considered the primary beneficiary. The Company determined that we are the primary beneficiary of the VIE and as a result are required to consolidate the VIE based on certain qualitative criteria such as, a principal/agency relationship existing between the parties with Brookstone qualifying as the principal, and the VIE's operations, products and design all being derived from Brookstone. The Company consolidated this entity effective for the first Fiscal quarter of 2004, which was the Company's first interim or annual reporting period ending after March 15, 2004, as required by this interpretation.

At July 4, 2009, January 3, 2009 and June 28, 2008, the following amounts were consolidated in the Company's balance sheet related to the Atlanta venture:

| | July 4, 2009 | January 3, 2009 | June 28, 2008 |
|--------------------------|--------------|-----------------|---------------|
| Assets | \$ 7,000 | \$ 20,000 | \$ 63,000 |
| Liabilities | - | - | - |
| Noncontrolling interests | 221,000 | 94,000 | 272,000 |

9. Retirement Plans

The Company sponsors both a defined benefit Pension Plan and a Postretirement Medical Benefit Plan. The Company estimates that contributions expected to be paid to the retirement plans during Fiscal 2009 are approximately \$127,000 for the Pension Plan and \$55,000 for the Postretirement Benefit Plan.

The components of net periodic benefit cost for the Pension Plan were as follows:

| | Thirteen weeks ended | | Twenty-six weeks ended | |
|--------------------------------|----------------------|------------------|------------------------|------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Service cost | \$ 31,000 | \$ 31,000 | \$ 62,000 | \$ 63,000 |
| Interest cost | 83,000 | 82,000 | 166,000 | 164,000 |
| Expected return on plan assets | (66,000) | (96,000) | (132,000) | (192,000) |
| Amortization of actuarial gain | 7,000 | (4,000) | 14,000 | (8,000) |
| Net periodic benefit cost | <u>\$ 55,000</u> | <u>\$ 13,000</u> | <u>\$ 110,000</u> | <u>\$ 27,000</u> |

The components of net periodic benefit cost (income) for the Postretirement Medical Benefit Plan were as follows:

| | Thirteen weeks ended | | Twenty-six weeks ended | |
|------------------------------------|----------------------|-------------------|------------------------|-------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Service cost | \$ --- | \$ --- | \$ --- | \$ --- |
| Interest cost | 9,000 | 9,000 | 18,000 | 18,000 |
| Amortization of prior service cost | (9,000) | (9,000) | (18,000) | (18,000) |
| Amortization of actuarial gain | (2,000) | (2,000) | (4,000) | (4,000) |
| Net periodic benefit income | <u>\$ (2,000)</u> | <u>\$ (2,000)</u> | <u>\$ (4,000)</u> | <u>\$ (4,000)</u> |

10. Debt

As of July 4, 2009, the Company had outstanding \$170 million in 12.0% Second Lien Senior Secured Notes due October 15, 2012. These notes bear interest at 12% per annum payable in semi-annual installments on April 15 and October 15 of each year.

The Company maintains a senior secured credit facility which provides up to \$125 million in available revolving borrowings subject to a borrowing base limitation and includes a letter of credit subfacility, a swingline subfacility and a stretch loan subfacility providing for increased advance rates on the borrowing base assets.

The Company expects 2009 will continue to be a challenging year due to the current conditions of the U.S. economy that have negatively impacted both consumer spending and traffic in retail malls across the country. As a result of these negative economic trends, the Company will become increasingly dependent on its senior secured credit facility in order to fund operations and finance our seasonal merchandise inventory build-up which has historically been during the third and fourth quarters.

Our borrowing base calculation is based on advance rates of eligible inventory and receivables. These advance rates vary during the course of the year and provide for increased availability during the Company's peak inventory purchasing season (third and fourth quarters). The Company anticipates that peak usage of its availability under the senior secured credit facility will occur during the earlier part of the fourth quarter.

Based on the foregoing, the Company believes its cash balances, cash funds expected to be generated by future operations, borrowing capacity and potential cost saving measures, if necessary, will be sufficient to fund operations through Fiscal 2009.

Borrowings under the senior secured credit facility bear interest at a rate equal to the sum of LIBOR (London Interbank Offer Rate) plus the applicable margin or, at our option, the alternate base rate (which will be the higher of (x) the Bank of America, N.A. prime rate and (y) the federal funds rate plus 0.50%) plus the

applicable margin. The applicable margin (other than with respect to the stretch loan subfacility) is adjusted from time to time in accordance with a pricing grid based on our average availability during the preceding fiscal quarter in excess of outstanding loans and extensions of credit under our senior secured credit facility. At July 4, 2009, the applicable margin, as amended, ranges from 1.00% to 1.50% per annum in the case of LIBOR rate advances (or in the case of the stretch loan subfacility, 4.0% per annum) and 0.00% per annum in the case of alternate base rate advances (or in the case of the stretch loan subfacility, 2.75% per annum). The default rate on our senior secured credit facility is 2% above the otherwise applicable interest rate.

The Company has a real estate loan on its headquarters facility and has a capital lease obligation on its Mexico, Missouri distribution center.

As of July 4, 2009, January 3, 2009 and June 28, 2008, the Company was in compliance with all related debt covenants and had cash borrowings outstanding under its senior secured credit facility in the amount of \$7 million, \$0 and \$0, respectively.

Derivative Financial Instruments

In order to minimize the risk of exposure related to variations in cash flows over the life of the financing on its headquarters facility, in August 2004, the Company entered into a \$4.0 million, 10-year interest rate swap agreement under which the Company receives one-month LIBOR plus 1.00% and pays a 5.67% fixed rate. The swap modifies the Company's interest rate exposure by effectively converting 50% of the real estate loan from a variable rate to a fixed rate in order to hedge against the possibility of rising interest rates during the term of the loan. While the swap agreement serves as an economic hedge, it does not qualify as an accounting hedge under SFAS No. 133. The fair value of the swap, as of July 4, 2009, January 3, 2009 and June 28, 2008 was approximately \$(135,000), \$(166,000) and \$(54,000), respectively, and was included in other long-term liabilities. Changes in the fair value of the swap are recorded in interest expense. See Note 5 for additional disclosure on fair value measurements.

11. Income Taxes

For the thirteen week period ended July 4, 2009, the Company recorded an income tax provision of \$0.1 million, as compared to an income tax benefit of \$5.3 million in the second quarter of Fiscal 2008. For the twenty-six week period ended July 4, 2009, the Company recorded an income tax provision of \$0.6 million, as compared to an income tax benefit of \$12.4 million in Fiscal 2008. The effective tax rate was (0.6)% and 39.1% for the thirteen-week period ended July 4, 2009 and June 28, 2008, respectively. The effective tax rate was (1.3)% and 38.6% for the twenty-six week period ended July 4, 2009 and June 28, 2008, respectively. The tax provision recorded in 2009, relates to amounts due in various states in which the Company has generated income, and an adjustment of certain estimates included in the reserve for uncertain tax positions. In addition, the Company recorded a valuation allowance of approximately \$15.6 million against the deferred tax assets generated in the first half of 2009.

12. Condensed Consolidating Financial Information

The following condensed consolidating financial information presents (1) Brookstone, Inc., the parent and a guarantor of the 12% Second Lien Senior Secured notes due 2012 (the “notes”), (2) Brookstone Company, Inc., the issuer of the notes, (3) Brookstone, Inc.’s guarantor subsidiaries of the notes (all of which are wholly-owned subsidiaries of Brookstone, Inc.) and (4) Brookstone, Inc.’s non-guarantor, non-wholly owned subsidiaries. Separate financial statements of the parent and guarantor subsidiaries are not presented because they are jointly, severally, fully and unconditionally liable under the guarantees. The investments in subsidiaries are accounted for under the equity basis of accounting.

Included in other expenses are revenues and expenses from management and royalty agreements among Brookstone, Inc. and its subsidiaries, which are eliminated in consolidation.

Brookstone, Inc.
Condensed Consolidating Balance Sheet
July 4, 2009
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|------------------------------------|-----------|------------|---------------------------|-------------------------------|--------------|--------------|
| Assets | | | | | | |
| Current assets: | | | | | | |
| Cash and cash equivalents | \$ --- | \$ 1,791 | \$ 226 | \$ 7 | \$ --- | \$ 2,024 |
| Receivables, net | --- | 3,644 | 2,984 | 100 | (100) | 6,628 |
| Merchandise inventories | --- | 14,484 | 51,446 | 162 | 150 | 66,242 |
| Deferred income taxes, net | --- | --- | --- | --- | --- | --- |
| Prepaid expenses | --- | 1,022 | 1,561 | --- | --- | 2,583 |
| Total current assets | --- | 20,941 | 56,217 | 269 | 50 | 77,477 |
| Property, plant and equipment, net | --- | 15,088 | 45,357 | 1,310 | --- | 61,755 |
| Intangible assets, net | --- | 105,000 | --- | --- | --- | 105,000 |
| Goodwill | --- | 99,734 | --- | --- | --- | 99,734 |
| Other assets | 73,699 | 92,053 | (9,810) | 1,486 | (150,338) | 7,090 |
| Total assets | \$ 73,699 | \$ 332,816 | \$ 91,764 | \$ 3,065 | \$ (150,288) | \$ 351,056 |
| Liabilities and Equity | | | | | | |
| Current liabilities: | | | | | | |
| Accounts payable | \$ --- | \$ 10,483 | \$ --- | \$ --- | \$ --- | \$ 10,483 |
| Other current liabilities | --- | 19,200 | 6,509 | 100 | (100) | 25,709 |
| Short-term borrowings | --- | 7,000 | --- | --- | --- | 7,000 |
| Total current liabilities | --- | 36,683 | 6,509 | 100 | (100) | 43,192 |
| Other long-term liabilities | --- | 11,657 | 82,350 | --- | (72,533) | 21,474 |
| Long-term debt | --- | 172,347 | 1,432 | --- | --- | 173,779 |
| Deferred income taxes | --- | 38,430 | (410) | --- | --- | 38,020 |
| Total liabilities | --- | 259,117 | 89,881 | 100 | (72,633) | 276,465 |
| Total equity | 73,699 | 73,699 | 1,883 | 2,965 | (77,655) | 74,591 |
| Total liabilities and equity | \$ 73,699 | \$ 332,816 | \$ 91,764 | \$ 3,065 | \$ (150,288) | \$ 351,056 |

Brookstone, Inc.
Consolidated Condensed Balance Sheet
January 3, 2009
(in thousands)

| | <u>Parent</u> | <u>Issuer</u> | <u>Guarantor Subsidiaries</u> | <u>Non- Guarantor Subsidiaries</u> | <u>Eliminations</u> | <u>Consolidated</u> |
|------------------------------------|-------------------|-------------------|-----------------------------------|--|---------------------|---------------------|
| Assets | | | | | | |
| Current assets: | | | | | | |
| Cash and cash equivalents | \$ - | \$ 22,005 | \$ 518 | \$ 7 | \$ - | \$ 22,530 |
| Receivables, net | - | 4,494 | 5,345 | 83 | (83) | 9,839 |
| Merchandise inventories | - | 12,151 | 69,456 | 166 | 322 | 82,095 |
| Prepaid expenses | - | 8,604 | 7,775 | - | - | 16,379 |
| Total current assets | - | 47,254 | 83,094 | 256 | 239 | 130,843 |
| Property, plant and equipment, net | - | 16,500 | 48,508 | 1,448 | - | 66,456 |
| Intangible assets, net | - | 105,000 | - | - | - | 105,000 |
| Goodwill | - | 99,734 | - | - | - | 99,734 |
| Other assets | 117,457 | 118,661 | (8,242) | 1,156 | (220,467) | 8,565 |
| Total assets | <u>\$ 117,457</u> | <u>\$ 387,149</u> | <u>\$ 123,360</u> | <u>\$ 2,860</u> | <u>\$ (220,228)</u> | <u>\$ 410,598</u> |
| Liabilities and Equity | | | | | | |
| Current liabilities: | | | | | | |
| Accounts payable | \$ - | \$ 17,033 | \$ - | \$ - | \$ - | \$ 17,033 |
| Other current liabilities | - | 23,094 | 18,085 | 83 | (83) | 41,179 |
| Total current liabilities | - | 40,127 | 18,085 | 83 | (83) | 58,212 |
| Other long term liabilities | - | 10,674 | 70,819 | - | (60,123) | 21,370 |
| Long term debt | - | 172,605 | 1,484 | - | - | 174,089 |
| Deferred income taxes | - | 46,286 | (7,856) | - | - | 38,430 |
| Total liabilities | - | 269,692 | 82,532 | 83 | (60,206) | 292,101 |
| Total equity | 117,457 | 117,457 | 40,828 | 2,777 | (160,022) | 118,497 |
| Total liabilities and equity | <u>\$ 117,457</u> | <u>\$ 387,149</u> | <u>\$ 123,360</u> | <u>\$ 2,860</u> | <u>\$ (220,228)</u> | <u>\$ 410,598</u> |

Brookstone, Inc.
Condensed Consolidating Balance Sheet
June 28, 2008
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|---------------------------------------|------------|------------|---------------------------|-------------------------------|--------------|--------------|
| Assets | | | | | | |
| Current assets: | | | | | | |
| Cash and cash equivalents | \$ --- | \$ 1,267 | \$ 291 | \$ 8 | \$ --- | \$ 1,566 |
| Receivables, net | --- | 4,835 | 3,848 | 178 | (178) | 8,683 |
| Merchandise inventories | --- | 19,588 | 72,106 | 161 | 267 | 92,122 |
| Deferred income taxes, net | --- | 12,864 | 3,938 | --- | --- | 16,802 |
| Prepaid expenses | --- | 2,330 | 8,741 | --- | --- | 11,071 |
| Total current assets | --- | 40,884 | 88,924 | 347 | 89 | 130,244 |
| Property, plant and equipment, net | --- | 16,912 | 52,065 | 1,386 | --- | 70,363 |
| Intangible assets, net | --- | 129,167 | --- | --- | --- | 129,167 |
| Goodwill | --- | 189,524 | --- | --- | --- | 189,524 |
| Other assets | 246,065 | 134,414 | 1,573 | 1,315 | (373,110) | 10,257 |
| Total assets | \$ 246,065 | \$ 510,901 | \$ 142,562 | \$ 3,048 | \$ (373,021) | \$ 529,555 |
| Liabilities and Equity | | | | | | |
| Current liabilities: | | | | | | |
| Accounts payable | \$ --- | \$ 14,947 | \$ --- | \$ --- | \$ --- | \$ 14,947 |
| Other current liabilities | --- | 20,449 | 9,534 | 178 | (178) | 29,983 |
| Total current liabilities | --- | 35,396 | 9,534 | 178 | (178) | 44,930 |
| Other long-term liabilities | --- | 9,304 | 76,508 | --- | (65,878) | 19,934 |
| Long-term debt | --- | 172,930 | 1,536 | --- | --- | 174,466 |
| Deferred income taxes | --- | 47,206 | (4,154) | --- | --- | 43,052 |
| Total liabilities | --- | 264,836 | 83,424 | 178 | (66,056) | 282,382 |
| Total equity | 246,065 | 246,065 | 59,138 | 2,870 | (306,965) | 247,173 |
| Total liabilities and equity | \$ 246,065 | \$ 510,901 | \$ 142,562 | \$ 3,048 | \$ (373,021) | \$ 529,555 |

Brookstone, Inc.
Condensed Consolidating Statement of Operations
For the thirteen-weeks ended July 4, 2009
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|--|--------------------|--------------------|---------------------------|-------------------------------|------------------|--------------------|
| Net sales | \$ --- | \$ 9,199 | \$ 60,443 | \$ 3,486 | \$ (156) | \$ 72,972 |
| Cost of sales | --- | 7,702 | 48,829 | 2,012 | (156) | 58,387 |
| Gross profit | --- | 1,497 | 11,614 | 1,474 | --- | 14,585 |
| Selling, general and administrative expenses | --- | 4,912 | 19,177 | 980 | --- | 25,069 |
| Other expenses (income) | --- | (7,233) | 7,233 | --- | --- | --- |
| Income (loss) from operations | --- | 3,818 | (14,796) | 494 | --- | (10,484) |
| Interest expense, net | --- | 5,893 | 99 | 3 | --- | 5,995 |
| Income (loss) before taxes | --- | (2,075) | (14,895) | 491 | --- | (16,479) |
| Income tax provision (benefit) | --- | 90 | 1 | --- | --- | 91 |
| Equity income in subsidiaries net of tax | (16,739) | (14,574) | 322 | --- | 30,991 | --- |
| Consolidated net income (loss) | (16,739) | (16,739) | (14,574) | 491 | 30,991 | (16,570) |
| Less: Net income attributable to noncontrolling interests | --- | --- | --- | 169 | --- | 169 |
| Net income (loss) attributable to Brookstone | <u>\$ (16,739)</u> | <u>\$ (16,739)</u> | <u>\$ (14,574)</u> | <u>\$ 322</u> | <u>\$ 30,991</u> | <u>\$ (16,739)</u> |

Brookstone, Inc.
Condensed Consolidating Statement of Operations
For the twenty-six weeks ended July 4, 2009
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|--|-------------|-------------|---------------------------|-------------------------------|--------------|--------------|
| Net sales | \$ --- | \$ 16,986 | \$ 112,215 | \$ 6,474 | \$ (1,244) | \$ 134,431 |
| Cost of sales | --- | 13,908 | 96,839 | 3,775 | (1,244) | 113,278 |
| Gross profit | --- | 3,078 | 15,376 | 2,699 | --- | 21,153 |
| Selling, general and administrative expenses | --- | 10,993 | 39,547 | 1,881 | --- | 52,421 |
| Other expenses (income) | --- | (15,542) | 15,542 | --- | --- | --- |
| Income (loss) from operations | --- | 7,627 | (39,713) | 818 | --- | (31,268) |
| Interest expense, net | --- | 11,748 | 220 | 7 | --- | 11,975 |
| Income (loss) before taxes | --- | (4,121) | (39,933) | 811 | --- | (43,243) |
| Income tax provision (benefit) | --- | 973 | (409) | --- | --- | 564 |
| Equity income in subsidiaries net of tax | (44,089) | (38,995) | 529 | --- | 82,555 | --- |
| Consolidated net income (loss) | (44,089) | (44,089) | (38,995) | 811 | 82,555 | (43,807) |
| Less: Net income attributable to noncontrolling interests | --- | --- | --- | 282 | --- | 282 |
| Net income (loss) attributable to Brookstone | \$ (44,089) | \$ (44,089) | \$ (38,995) | \$ 529 | \$ 82,555 | \$ (44,089) |

Brookstone, Inc.
Condensed Consolidating Statement of Operations
For the thirteen-weeks ended June 28, 2008
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|---|------------|------------|---------------------------|-------------------------------|--------------|--------------|
| Net sales | \$ --- | \$ 12,390 | \$ 80,822 | \$ 4,463 | \$ (285) | \$ 97,390 |
| Cost of sales | --- | 9,596 | 59,248 | 2,317 | (285) | 70,876 |
| Gross profit | --- | 2,794 | 21,574 | 2,146 | --- | 26,514 |
| Selling, general and administrative expenses | --- | 5,655 | 27,401 | 1,176 | --- | 34,232 |
| Other expenses (income) | --- | (7,250) | 7,250 | --- | --- | --- |
| Income (loss) from operations | --- | 4,389 | (13,077) | 970 | --- | (7,718) |
| Interest expense, net | --- | 5,804 | 95 | 3 | --- | 5,902 |
| Income (loss) before taxes | --- | (1,415) | (13,172) | 967 | --- | (13,620) |
| Income tax provision (benefit) | --- | (518) | (4,810) | --- | --- | (5,328) |
| Equity income in subsidiaries net of tax | (8,662) | (7,765) | 597 | --- | 15,830 | --- |
| Consolidated net income (loss) | (8,662) | (8,662) | (7,765) | 967 | 15,830 | (8,292) |
| Less: Net income (loss) attributable to noncontrolling interests | --- | --- | --- | 370 | --- | 370 |
| Net income (loss) attributable to Brookstone | \$ (8,662) | \$ (8,662) | \$ (7,765) | \$ 597 | \$ 15,830 | \$ (8,662) |

Brookstone, Inc.
Condensed Consolidating Statement of Operations
For the twenty-six weeks ended June 28, 2008
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|---|-------------|-------------|---------------------------|-------------------------------|--------------|--------------|
| Net sales | \$ --- | \$ 24,432 | \$ 154,651 | \$ 8,242 | \$ (134) | \$ 187,191 |
| Cost of sales | --- | 19,038 | 115,547 | 4,441 | (134) | 138,892 |
| Gross profit | --- | 5,394 | 39,104 | 3,801 | --- | 48,299 |
| Selling, general and administrative expenses | --- | 12,059 | 54,782 | 2,126 | --- | 68,967 |
| Other expenses (income) | --- | (15,437) | 15,437 | --- | --- | --- |
| Income (loss) from operations | --- | 8,772 | (31,115) | 1,675 | --- | (20,668) |
| Interest expense, net | --- | 11,294 | 224 | 6 | --- | 11,524 |
| Income (loss) before taxes | --- | (2,522) | (31,339) | 1,669 | --- | (32,192) |
| Income tax provision (benefit) | --- | (941) | (11,494) | --- | --- | (12,435) |
| Equity income in subsidiaries net of tax | (20,393) | (18,812) | 1,033 | --- | 38,172 | --- |
| Consolidated net income (loss) | (20,393) | (20,393) | (18,812) | 1,669 | 38,172 | (19,757) |
| Less: Net income attributable to noncontrolling interests | --- | --- | --- | 636 | --- | 636 |
| Net income (loss) attributable to Brookstone | \$ (20,393) | \$ (20,393) | \$ (18,812) | \$ 1,033 | \$ 38,172 | \$ (20,393) |

Brookstone, Inc.
Condensed Consolidating Statement of Cash Flows
For the twenty-six weeks ended July 4, 2009
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|--|-------------|-------------|---------------------------|-------------------------------|--------------|--------------|
| Cash flows from operating activities: | | | | | | |
| Consolidated net income (loss) | \$ (44,089) | \$ (44,089) | \$ (38,995) | \$ 811 | \$ 82,555 | \$ (43,807) |
| Adjustments to reconcile consolidated net income (loss) to net cash used for operating activities: | | | | | | |
| Depreciation and amortization | --- | 1,362 | 5,673 | 214 | --- | 7,249 |
| Amortization of debt issuance costs | --- | 1,069 | --- | --- | --- | 1,069 |
| Amortization of debt discount | --- | 141 | --- | --- | --- | 141 |
| Amortization of revaluation of leases | --- | (13) | (63) | --- | --- | (76) |
| Loss on disposal of property, plant and equipment | --- | --- | 139 | --- | --- | 139 |
| Share-based compensation | --- | 341 | --- | --- | --- | 341 |
| Deferred income taxes, net | --- | (7,856) | 7,446 | --- | --- | (410) |
| Equity income in subsidiary | 44,089 | 38,995 | (529) | --- | (82,555) | --- |
| Changes in operating assets and liabilities: | | | | | | |
| Accounts receivable, net | --- | 850 | 2,361 | (47) | 17 | 3,181 |
| Merchandise inventories | --- | (2,333) | 18,010 | 4 | 172 | 15,853 |
| Prepaid expenses | --- | 7,582 | 6,214 | --- | --- | 13,796 |
| Other assets | --- | (13,482) | 1,879 | (523) | 12,238 | 112 |
| Accounts payable | --- | (6,550) | --- | --- | --- | (6,550) |
| Other current liabilities | --- | (3,894) | (11,576) | 17 | (17) | (15,470) |
| Other long-term liabilities | --- | 1,012 | 11,862 | --- | (12,410) | 464 |
| Net cash provided by (used for) operating activities | --- | (26,865) | 2,421 | 476 | --- | (23,968) |
| Cash flows from investing activities: | | | | | | |
| Expenditures for property, plant and equipment, net | --- | 50 | (2,661) | (76) | --- | (2,687) |
| Net cash (used for) provided by investing activities | --- | 50 | (2,661) | (76) | --- | (2,687) |
| Cash flows from financing activities: | | | | | | |
| Borrowings from senior secured credit facility, net | --- | 7,000 | --- | --- | --- | 7,000 |
| Payments on long-term debt and capital lease | --- | (399) | (52) | --- | --- | (451) |
| Cash contributions by noncontrolling interests | --- | --- | --- | 48 | --- | 48 |
| Cash distributions to noncontrolling interests | --- | --- | --- | (448) | --- | (448) |
| Net cash used for financing activities | --- | 6,601 | (52) | (400) | --- | (6,149) |
| Net decrease in cash and cash equivalents | --- | (20,214) | (292) | --- | --- | (20,506) |
| Cash and cash equivalents at beginning of period | --- | 22,005 | 518 | 7 | --- | 22,530 |
| Cash and cash equivalents at end of period | \$ --- | \$ 1,791 | \$ 226 | \$ 7 | \$ --- | \$ 2,024 |

Brookstone, Inc.
Condensed Consolidating Statement of Cash Flows
For the twenty-six weeks ended June 28, 2008
(In thousands)
(Unaudited)

| | Parent | Issuer | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | Consolidated |
|--|-------------|-------------|---------------------------|-------------------------------|--------------|--------------|
| Cash flows from operating activities: | | | | | | |
| Consolidated net income (loss) | \$ (20,393) | \$ (20,393) | \$ (18,812) | \$ 1,669 | \$ 38,172 | \$ (19,757) |
| Adjustments to reconcile consolidated net income (loss) to net cash used for operating activities: | | | | | | |
| Depreciation and amortization | --- | 1,590 | 5,906 | 189 | --- | 7,685 |
| Amortization of debt issuance costs | --- | 1,068 | --- | --- | --- | 1,068 |
| Amortization of debt discount | --- | 141 | --- | --- | --- | 141 |
| Amortization of revaluation of leases | --- | 11 | (40) | --- | --- | (29) |
| Loss on disposal of property, plant and equipment | --- | 11 | 561 | --- | --- | 572 |
| Share-based compensation | --- | (214) | --- | --- | --- | (214) |
| Deferred income taxes, net | --- | (12,610) | 38 | --- | --- | (12,572) |
| Equity income in subsidiary | 20,393 | 18,812 | (1,033) | --- | (38,172) | --- |
| Changes in operating assets and liabilities: | | | | | | |
| Accounts receivable, net | --- | (96) | 4,229 | (44) | 178 | 4,267 |
| Merchandise inventories | --- | (4,464) | 18,751 | 18 | (27) | 14,278 |
| Prepaid expenses | --- | (1,431) | (5,620) | --- | --- | (7,051) |
| Other assets | --- | (18,409) | (22,165) | (417) | 41,110 | 119 |
| Accounts payable | --- | (18,560) | --- | --- | --- | (18,560) |
| Other current liabilities | --- | (13,881) | (17,350) | 178 | (178) | (31,231) |
| Other long-term liabilities | --- | 261 | 40,640 | --- | (41,083) | (182) |
| Net cash provided by (used for) operating activities | --- | (68,164) | 5,105 | 1,593 | --- | (61,466) |
| Cash flows from investing activities: | | | | | | |
| Expenditures for property, plant and equipment, net | --- | (506) | (5,275) | (680) | --- | (6,461) |
| Net cash (used for) provided by investing activities | --- | (506) | (5,275) | (680) | --- | (6,461) |
| Cash flows from financing activities: | | | | | | |
| Payments on long-term debt and capital lease | --- | (400) | (52) | --- | --- | (452) |
| Cash contributions by noncontrolling interests | --- | --- | --- | 253 | --- | 253 |
| Cash distributions to noncontrolling interests | --- | --- | --- | (1,165) | --- | (1,165) |
| Net cash used for financing activities | --- | (400) | (52) | (912) | --- | (1,364) |
| Net decrease in cash and cash equivalents | --- | (69,070) | (222) | 1 | --- | (69,291) |
| Cash and cash equivalents at beginning of period | --- | 70,337 | 513 | 7 | --- | 70,857 |
| Cash and cash equivalents at end of period | \$ --- | \$ 1,267 | \$ 291 | \$ 8 | \$ --- | \$ 1,566 |

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

Forward-Looking Statements

This Quarterly Report on Form 10-Q and, in particular, this Management's Discussion and Analysis contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Readers can identify these statements by forward-looking words such as "may," "could," "should," "would," "intend," "will," "expect," "anticipate," "believe," "estimate," "continue" or similar words. Readers should carefully review statements that contain these words because they discuss our future expectations, contain projections of our future results of operations or of our financial condition or state other "forward-looking" information. We caution investors that all such forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from any projected results or expectations that we discuss in this report. You should therefore carefully review the risk factors and uncertainties discussed in Item 1A of our most recent Annual Report on Form 10-K for Fiscal 2008, as posted to our web site at www.brookstone.com, as well as those factors that are otherwise described from time to time in Brookstone's reports posted on its website after this report. We undertake no obligation to update any forward-looking statements.

General

Founded in 1965, Brookstone is a leading nationwide specialty retailer. Our strategy is to develop unique, innovative, Brookstone-branded products, and to procure unique products from other sources, and offer them for sale to customers via our proprietary distribution channels, which consist of our retail stores, our internet website and our catalogs. Our products are intended to make some aspect of our customer's life easier, better, more enjoyable or more fun, qualities that we believe make our products particularly well suited for gift giving.

The Company operates in two reportable segments based on its two distinct distribution channels; Retail and Direct Marketing. The Retail segment is comprised of all full-year stores in addition to all temporary stores and kiosks. Retail product distribution is conducted primarily through the store locations. The Direct Marketing segment is comprised of the *Brookstone* catalog and products promoted via our internet website, www.brookstone.com and sales to corporate and wholesale customers. Direct Marketing product distribution is primarily conducted through the Company's distribution center located in Mexico, Missouri and by its vendors.

This Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to provide information to assist you in better understanding our business. We recommend that you read this MD&A in conjunction with the unaudited Consolidated Financial Statements and the accompanying notes to these statements and our Annual Report on Form 10-K for the fiscal year ended January 3, 2009. The purposes of this MD&A include providing to the reader the perspectives of management as we view the business and providing you with insights that are not necessarily obvious or clear from reading our Consolidated Financial Statements (including Notes) alone.

Results of Operations

Overview - The Company's results of operations for the first half of 2009 were adversely impacted by the current conditions of the U.S. economy. The current economic trends have negatively impacted both consumer spending and traffic in retail malls across the country. It is unclear to what extent these conditions will persist and what overall impact they will have on future consumer spending, as compared to our expectations.

We responded to these economic conditions at the end of 2008 with a planned reduction of \$30 million in overall operating expenses for 2009, including a reduction of 15% in corporate headcount and a freeze on all discretionary capital spending. Through the end of the second quarter of 2009, we have reduced operating expenses by \$16.5 million, and are on track to meet, if not exceed, our expense reduction goals for the year. Additionally, we have effectively managed our inventory levels throughout the year, resulting in a 28% decrease at the end of the second quarter of 2009 as compared to the second quarter of last year.

These actions have had a positive effect on managing our cash position. After beginning the year \$48.3 million below the prior year's cash levels, our short-term net borrowings at July 4, 2009, were only \$6.5 million higher than the second quarter of 2008. In addition, we had approximately \$34.1 million of availability under our revolving credit facility, which is in place through October of 2010.

Operating results as a % of net sales - The Company has provided the following statistical summary of its operating results as we have incorporated this information into the discussion below in order to assist the reader in understanding the Company's results of operations on a comparative basis and in recognizing underlying trends.

| | Thirteen weeks ended | | Twenty-six weeks ended | |
|---|----------------------|---------------|------------------------|----------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Net sales | | | | |
| Retail segment | 83.8% | 79.4% | 83.7% | 80.3% |
| Direct Marketing segment | 16.2 | 20.6 | 16.3 | 19.7 |
| Total net sales | 100.0 | 100.0 | 100.0 | 100.0 |
| Cost and expenses: | | | | |
| Cost of sales | 80.0 | 72.8 | 84.3 | 74.2 |
| Gross profit | 20.0 | 27.2 | 15.7 | 25.8 |
| Selling, general and administrative expenses | 34.4 | 35.1 | 39.0 | 36.8 |
| Loss from operations | (14.4) | (7.9) | (23.3) | (11.0) |
| Interest expense, net | 8.2 | 6.1 | 8.9 | 6.2 |
| Loss before income taxes | (22.6) | (14.0) | (32.2) | (17.2) |
| Income tax provision (benefit) | 0.1 | (5.5) | 0.4 | (6.6) |
| Consolidated net loss | (22.7) | (8.5) | (32.6) | (10.6) |
| Less: Net income attributable to noncontrolling interests | 0.2 | 0.4 | 0.2 | 0.3 |
| Net loss attributable to Brookstone | <u>(22.9)%</u> | <u>(8.9)%</u> | <u>(32.8)%</u> | <u>(10.9)%</u> |

Net Sales - For the thirteen week period ended July 4, 2009, net sales decreased 25.1% to \$73.0 million as compared to the second quarter of 2008. For the twenty-six week period ended July 4, 2009, net sales decreased 28.2% to \$134.4 million as compared to the twenty-six week period in Fiscal 2008. Same-store sales decreased 18.6% and 21.6% for the thirteen and twenty-six week periods ended July 4, 2009, respectively.

The decrease in same-store sales was largely driven by the weak current economic environment, which has negatively impacted both consumer spending and traffic in retail malls across the country.

Retail segment - For the thirteen week period ended July 4, 2009, net sales in the Retail segment decreased \$16.2 million, or 20.9%, to \$61.1 million as compared to \$77.3 million for the second quarter of last year. For the twenty-six week period ended July 4, 2009, net sales in the Retail segment decreased \$37.8 million, or 25.1%, to \$112.5 million as compared to \$150.3 million for the twenty-six week period in 2008. The decreases in both periods are primarily the result of the same-store sales decrease, and sales reductions resulting from the closing of 14 stores, partially offset by the opening of 10 new stores, subsequent to the second quarter of 2008. The total number of Brookstone stores open on July 4, 2009 was 310 versus 314 on June 28, 2008.

Direct Marketing segment - For the thirteen week period ended July 4, 2009, Direct Marketing sales decreased \$8.3 million or 41.1% to \$11.8 million as compared to \$20.1 million for the second quarter of 2008, primarily due to decreases in revenue resulting from a 56% reduction in catalog circulation and reduced consumer response. The decrease includes a decrease of \$1.3 million in revenues generated from customers for shipping and handling. For the twenty-six week period ended July 4, 2009, Direct Marketing sales decreased \$15.0 million or

40.6% to \$21.9 million as compared to \$36.9 million for the twenty-six week period in 2008, primarily due to decreases in revenue resulting from a 52% reduction in catalog circulation and reduced consumer response. The decrease includes a decrease of \$2.2 million in revenues generated from customers for shipping and handling.

Gross profit - For the thirteen week period ended July 4, 2009, gross profit as a percentage of net sales decreased 7.2% to 20.0% versus 27.2% for the second quarter of 2008. This decrease is a result of an increase in occupancy costs as a percentage of sales of 6.4%, a decrease in product margins as a percentage of sales of 2.2%, offset by a decrease of 1.4% as a percentage of sales in order postage expense (costs associated with the delivery of products to customers). For the twenty-six week period ended July 4, 2009, gross profit as a percentage of net sales decreased 10.1% to 15.7% versus 25.8% for the twenty-six week period in Fiscal 2008. This decrease is a result of an increase in occupancy costs as a percentage of sales of 8.6%, a decrease in product margins as a percentage of sales of 2.5%, offset by a decrease of 1.0% as a percentage of sales in order postage expense. Occupancy costs as a percentage of net sales increased in both periods, primarily as a result of the decrease in sales. The decrease in product margins as a percentage of net sales in both periods was primarily due to increased promotional activity.

Selling, General & Administrative expenses - For the thirteen week period ended July 4, 2009, selling, general and administrative expenses as a percentage of net sales decreased 0.7% to 34.4% versus 35.1% for the second quarter of Fiscal 2008, primarily as a result of a decrease in advertising as a percentage of net sales of 3.3% and a decrease of 1.1% in general administrative costs, offset by an increase in payroll costs as a percentage of net sales of 3.7%. For the twenty-six week period ended July 4, 2009, selling, general and administrative expenses as a percentage of net sales increased 2.2% to 39.0% versus 36.8% for the twenty-six week period in Fiscal 2008, primarily as a result of an increase in payroll costs as percentage of net sales of 5.8%, offset by a decrease in advertising of 2.8%, and a decrease of 0.8% in general administrative costs. While SG&A expenses increased as a percentage of net sales due to the overall decrease in sales, these expenses actually decreased in the first half of 2009 approximately \$16.5 million as compared to the first half of 2008, as a result of the cost reductions that were implemented at the end of Fiscal 2008.

Loss from operations - As a result of the foregoing, for the thirteen and twenty-six week periods ended July 4, 2009, the Company reported a loss from operations of \$10.5 million and \$31.3 million, respectively, as compared to a loss from operations of \$7.7 million and \$20.7 million for the thirteen and twenty-six week periods ended June 28, 2008, respectively.

Interest expense, net - For the thirteen week period ended July 4, 2009, net interest expense was \$6.0 million, compared to \$5.9 million for the second quarter of Fiscal 2008. For the twenty-six week period ended July 4, 2009, net interest expense was \$12.0 million as compared to \$11.5 million for the twenty-six week period in Fiscal 2008. The increase in net interest expense in both periods is primarily due to reduced interest income as a result of the Company having less available cash for investment.

Income taxes - For the thirteen week period ended July 4, 2009, the Company recorded an income tax provision of \$0.1 million, as compared to an income tax benefit of \$5.3 million in the second quarter of Fiscal 2008. For the twenty-six week period ended July 4, 2009, the Company recorded an income tax provision of \$0.6 million, as compared to an income tax benefit of \$12.4 million in Fiscal 2008. The effective tax rate was (0.6)% and 39.1% for the thirteen-week period ended July 4, 2009 and June 28, 2008, respectively. The effective tax rate was (1.3)% and 38.6% for the twenty-six week period ended July 4, 2009 and June 28, 2008, respectively. The tax provision recorded in 2009, relates to amounts due in various states in which the Company has generated income, and an adjustment of certain estimates included in the reserve for uncertain tax positions. In addition, the Company recorded a valuation allowance of approximately \$15.6 million against the deferred tax assets generated in the first half of 2009.

Consolidated net loss - Overall, for the thirteen and twenty-six week periods ended July 4, 2009, the Company reported a consolidated net loss of \$16.6 million and \$43.8 million, respectively, as compared to a net loss of \$8.3 million and \$19.8 million for the thirteen and twenty-six week periods ended June 28, 2008, respectively.

Financial Condition, Liquidity and Capital Resources

Cash flows for the twenty-six week period ended July 4, 2009

For the twenty-six week period ended July 4, 2009, the Company's cash position decreased \$20.5 million to \$2.0 million. Cash used for operations totaled \$24.0 million, primarily as a result of the Company's net loss from operations, payments made for merchandise purchases during the 2008 winter holiday selling season, and a decrease in other current liabilities resulting primarily from decreased returns from customers and the payment of sales taxes. These cash outflows were partially offset by a decrease in receivables, primarily as a result of payments received from fourth quarter sales on credit and receipts of construction allowances from landlords, the receipt of federal tax refunds, the timing of certain prepaid expenses, and lower inventory levels due to reduced merchandise purchases during the first half of 2009.

Cash of \$2.7 million was utilized to fund capital expenditures in the twenty-six week period ended July 4, 2009, primarily related to the development of our new website and the remodeling of three Brookstone stores.

Net cash provided by financing activities totaled approximately \$6.1 million in the twenty-six week period ended July 4, 2009, reflecting net borrowings from our senior secured credit facility, payments on long-term debt and net distributions to non controlling interests.

Cash flows for the twenty-six week period ended June 28, 2008

For the twenty-six week period ended June 28, 2008, the Company's cash position decreased \$69.3 million to \$1.6 million. Cash used for operations totaled \$61.5 million, primarily as a result of payments made for merchandise purchases during the 2007 winter holiday selling season and the first six months of 2008, the Company's net loss from operations and a decrease in other current liabilities resulting primarily from decreased returns from customers and the payment of sales and income taxes. These cash outflows were partially offset by a decrease in receivables, primarily as a result of payments received from fourth quarter sales on credit, and lower inventory levels due to reduced merchandise purchases during the first half of 2008.

Cash of \$6.5 million was utilized to fund capital expenditures in the twenty-six week period ended June 28, 2008, primarily related to the opening of five new Brookstone stores, the remodeling of seven Brookstone stores and construction related to stores opened or remodeled in the fiscal year.

Net cash used for financing activities totaled approximately \$1.4 million in the twenty-six week period ended June 28, 2008, reflecting payments on long-term debt and net distributions to noncontrolling interests.

Outlook

The Company expects 2009 will continue to be a challenging year due to the current conditions of the U.S. economy that have negatively impacted both consumer spending and traffic in retail malls across the country. As a result of these negative economic trends, the Company will become increasingly dependent on its senior secured credit facility in order to fund operations and finance our seasonal merchandise inventory build-up which has historically been during the third and fourth quarters.

Our senior secured credit facility, which expires on October 4, 2010, provides us with up to \$125 million in available borrowings subject to a borrowing base limitation. Our borrowing base calculation is based on advance rates of eligible inventory and receivables. These advance rates vary during the course of the year and provide for increased availability during the Company's peak inventory purchasing season (third and fourth quarters). Our senior secured credit facility contains a minimum fixed charge coverage ratio covenant that will be triggered if availability under the senior secured credit facility falls below \$20 million. The Company anticipates that peak usage of its availability under the senior secured credit facility will occur during the earlier part of the fourth quarter.

Based on the foregoing, the Company believes its cash balances, cash funds expected to be generated by future operations, borrowing capacity and potential cost saving measures, if necessary, will be sufficient to fund operations through Fiscal 2009.

Recent Accounting Pronouncements

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 168, *The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles a Replacement of FASB Statement No. 162*. This Standard establishes the FASB Accounting Standards Codification™ (the “Codification”) as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. GAAP. The Codification does not change current U.S. GAAP, but is intended to simplify user access to all authoritative U.S. GAAP by providing all the authoritative literature related to a particular topic in one place. The Codification is effective for interim and annual periods ending after September 15, 2009, and as of the effective date, all existing accounting standard documents will be superseded. The Codification is effective for our Company in the third quarter of 2009, and accordingly, our Quarterly Report on Form 10-Q for the quarter ending October 3, 2009 and all subsequent financial statements will reference the Codification as the sole source of authoritative literature.

In June 2009, the FASB issued SFAS No. 167, *Amendments to FASB Interpretation No. 46(R)*, which modifies how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. SFAS 167 clarifies that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity’s purpose and design and a company’s ability to direct the activities of the entity that most significantly impact the entity’s economic performance. SFAS 167 requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity. SFAS 167 also requires additional disclosures about a company’s involvement in variable interest entities and any significant changes in risk exposure due to that involvement. SFAS 167 is effective for fiscal years beginning after November 15, 2009. We have not completed our assessment of the impact SFAS 167 will have on our consolidated financial statements.

In June 2009, the FASB issued SFAS No. 166, *Accounting for Transfers of Financial Assets — an amendment of FASB Statement No. 140*, which requires entities to provide more information regarding sales of securitized financial assets and similar transactions, particularly if the entity has continuing exposure to the risks related to transferred financial assets. SFAS 166 eliminates the concept of a “qualifying special-purpose entity,” changes the requirements for derecognizing financial assets and requires additional disclosures. SFAS 166 is effective for fiscal years beginning after November 15, 2009. We have not completed our assessment of the impact SFAS 166 will have on our consolidated financial statements, if any.

In May 2009, the FASB issued SFAS No. 165, *Subsequent Events*, which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. SFAS 165 also requires entities to disclose the date through which subsequent events were evaluated as well as the rationale for why that date was selected. SFAS 165 is effective for interim and annual periods ending after June 15, 2009, and accordingly, we adopted this Standard during the second quarter of 2009. SFAS 165 requires that public entities evaluate subsequent events through the date that the financial statements are issued. We have evaluated subsequent events through the time of the posting of these financial statements to our website at www.brookstone.com on August 14, 2009.

In April 2009, the FASB issued FASB Staff Position (FSP) FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*. This FSP requires disclosures about the fair value of financial instruments whenever a public company issues financial information for interim reporting periods. This FSP was effective for our Company on April 5, 2009. The adoption of FSP FAS 107-1 and APB 28-1 did not have a significant impact to our consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133*. SFAS No. 161 applies to all derivative instruments and related hedged items accounted for under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS No. 133). SFAS No. 161 requires entities to provide greater transparency about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity’s financial position, results of operations and cash flows. SFAS No. 161 was effective for our Company on January 4, 2009. The adoption of SFAS No. 161 did not have a significant impact to our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements — an amendment of Accounting Research Bulletin No. 51*. SFAS No. 160 establishes accounting and reporting standards for noncontrolling interests (previously referred to as minority interests) in subsidiaries. SFAS No. 160 requires that a noncontrolling interest in a subsidiary should be accounted for as a component of equity separate from the parent's equity, rather than as a liability. SFAS No. 160 was effective for our Company on January 4, 2009, and is being applied prospectively, except for the presentation and disclosure requirements, which have been applied retrospectively. The adoption of SFAS No. 160 altered the presentation of noncontrolling interests in our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations*. SFAS No. 141(R) amends the principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree and the goodwill acquired. SFAS No. 141(R) also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. SFAS No. 141(R) was effective for our Company on January 4, 2009, and the Company will apply SFAS No. 141(R) prospectively to all business combinations subsequent to the effective date. The adoption of SFAS No. 141(R) did not have a significant impact on our consolidated financial statements, and the impact that its adoption will have on our consolidated financial statements in future periods will depend on the nature and size of business combinations completed subsequent to the date of adoption.

Critical Accounting Policies

The preparation of the Company's consolidated financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenue and expense during the reporting periods. Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 2 of the Notes to Consolidated Financial Statements in the Company's Annual Report on Form 10-K for the year ended January 3, 2009, as posted on the Company's website at www.brookstone.com, describe the significant accounting policies and critical accounting estimates used in the preparation of the consolidated financial statements. The Company's management is required to make judgments and estimates about the effect of matters that are inherently uncertain. Actual results could differ from management's estimates. With the exception of our adoption of SFAS No. 160, which altered the presentation of noncontrolling interests in our consolidated financial statements, there have been no material changes to our application of critical accounting policies and significant judgments and estimates since January 3, 2009.

ITEM 3. *Quantitative and Qualitative Disclosures about Market Risk.*

The Company's primary market risk is its interest rate risk. The Company does not engage in trading activities and its foreign currency risk and commodity price risk is immaterial.

The Company's interest rate exposure is most sensitive to fluctuations in interest rates in the United States, which impact interest paid on its debt. A 10% change in the weighted average interest rate on the Company's variable rate debt would be immaterial to the Company's consolidated financial positions, results of operations and cash flows.

The Company's Fiscal 2008 annual report on Form 10-K, as posted on the Company's website at www.brookstone.com, also contains information about market risks under "Item 7A. Quantitative and Qualitative Disclosures About Market Risk." There have been no material changes in our exposure to market risks during the thirteen weeks ended July 4, 2009.

ITEM 4T. *Controls and Procedures.*

The Company carried out an evaluation, under the supervision and with the participation of the Company's Disclosure Committee and the Company's management, including the Interim Chief Executive Officer and the Vice President, Finance, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of July 4, 2009 pursuant to Exchange Act Rule 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934. Based upon that evaluation, the Interim Chief Executive Officer and the Vice President, Finance, concluded that the Company's disclosure controls and procedures are effective. There have not been any changes in the Company's internal controls over financial reporting that have occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

PART II

OTHER INFORMATION

ITEM 1. *Legal Proceedings.*

Alvarez, et al. v. Brookstone Co., Inc.

As previously reported in our Annual Report on Form 10-K for fiscal year 2008, on December 10, 2008, a putative class action was commenced against us in California Superior Court for San Diego County. The complaint and subsequently filed amended complaint alleged, among other things, that we violated the California Credit Card Act of 1971 by requesting that customers using credit cards provide "personal identification information" in the form of zip codes. The Plaintiff also alleged an invasion of the right to privacy protected by the California Constitution. In addition to statutory and other unspecified damages, the lawsuit sought injunctive relief and an award of attorneys' fees. On July 27, 2009, the Court sustained our demurrer to all of the claims in the amended complaint without leave to amend. We do not know whether the Plaintiff will seek to appeal this ruling.

As of July 4, 2009, the end of the quarterly period covered by this report, we were subject to the various legal proceedings and claims discussed above, as well as certain other legal proceedings and claims that have not been fully resolved and that have arisen in the ordinary course of business. In the opinion of management, we do not have a potential liability related to any current legal proceedings and claims that would individually or in the aggregate have a material adverse effect on its financial condition or operating results. However, the results of legal proceedings cannot be predicted with certainty. Should we fail to prevail in any of these legal matters or should several of these legal matters be resolved against us in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

ITEM 1A. *Risk Factors*

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Item 1A of our most recent Annual Report on Form 10-K for Fiscal 2008, as posted to our web site at www.brookstone.com. These and other risks could materially and adversely affect our business, results of operations or financial condition. There have been no material changes from the risk factors previously disclosed in our most recent Annual Report on Form 10-K.

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

None.

ITEM 3. *Defaults Upon Senior Securities.*

None.

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

On July 22, 2009, the Company engaged in a solicitation of the Holders of its 12% Second Lien Senior Secured Notes Due 2012, in which the following matter was submitted to a vote of such Holders:

- The Company requested approval of the Holders of a majority in aggregate principal amount of outstanding Notes to waive the requirement of Section 4.03(a) of the Indenture dated as of October 4, 2005 among Brookstone Company, Inc., the Guarantors (as defined in the Indenture), and Wells Fargo Bank, N.A., as trustee, to the extent that it requires the Company to comply with Section 404(b) of the Sarbanes-Oxley Act of 2002, with respect to its annual report for the fiscal year ended January 2, 2010. Section 404(b) requires that the Company's independent auditors attest to, and report on, the Company's internal control over financial reporting. The Company will continue to comply with Section 404(a), which requires management of the Company to assess and report on the effectiveness of the Company's internal control over financial reporting.

This waiver was approved by the following vote representing the principal amount of notes outstanding:

| | |
|---------------------------|------------|
| Votes to grant the waiver | 91,461,011 |
| Votes withheld | 10,532,000 |
| No-votes | 68,006,989 |

ITEM 5. *Other Information.*

None.

ITEM 6. *Exhibits.*

- 31.1 Certification of Principal Executive Officer in the Form Provided by Rule 15d-14 of the Securities Exchange Act of 1934 (filed herewith)
- 31.2 Certification of Principal Financial Officer in the Form Provided by Rule 15d-14 of the Securities Exchange Act of 1934 (filed herewith)
- 32.1 Certification of Interim Chief Executive Officer in the Form Provided by Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)
- 32.2 Certification of Vice President, Finance in the Form Provided by Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

Signatures

Pursuant to the requirements of the Indenture, dated as of October 4, 2005, among Brookstone, Inc., Brookstone Company, Inc., the Guarantors (as defined therein) and Wells Fargo Bank, N.A., as Trustee, the Company has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized on August 14, 2009.

Brookstone, Inc.

/s/ Thomas F. Moynihan
(Signature)

Thomas F. Moynihan
Vice President, Finance
(Principal Financial Officer
and duly authorized to sign on behalf of the Company)

Exhibit Index

**Exhibit
Number**

Exhibit

- | | |
|------|--|
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| 32.2 | Certification of Vice President, Finance in the Form Provided by Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith) |

**Certification in the Form Provided by Rule 15d-14
of the Securities Exchange Act of 1934**

I, Philip W. Roizin, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the period ended July 4, 2009 of Brookstone, Inc.;
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 company as of, and for, the periods presented in this report;
4. The company'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 company 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 company, 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 company'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 company's internal control over financial reporting that occurred during the company's most recent fiscal quarter (the company's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of company'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 company'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 company's internal control over financial reporting.

Date: August 14, 2009

By: /s/ Philip W. Roizin
Philip W. Roizin
Interim President and Chief Executive Officer
(Principal Executive Officer)

**Certification in the Form Provided by Rule 15d-14
of the Securities Exchange Act of 1934**

I, Thomas F. Moynihan, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the period ended July 4, 2009 of Brookstone, Inc.;
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 company as of, and for, the periods presented in this report;
4. The company'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 company 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 company, 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 company'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 company's internal control over financial reporting that occurred during the company's most recent fiscal quarter (the company's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of company'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 company'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 company's internal control over financial reporting.

Date: August 14, 2009

By: /s/ Thomas F. Moynihan
Thomas F. Moynihan
Vice President, Finance
(Principal Financial Officer)

**CERTIFICATION IN THE FORM PROVIDED BY
SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, as Interim President and Chief Executive Officer of Brookstone, Inc. (the "Company"), does hereby certify that to the undersigned's knowledge:

- 1) the Company's Form 10-Q for the quarterly period ended July 4, 2009 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 Company's Form 10-Q for the quarterly period ended July 4, 2009 fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Philip W. Roizin

Philip W. Roizin
Interim President and Chief Executive Officer

Dated: August 14, 2009

**CERTIFICATION IN THE FORM PROVIDED BY
SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, as Vice President, Finance of Brookstone, Inc. (the "Company"), does hereby certify that to the undersigned's knowledge:

- 1) the Company's Form 10-Q for the quarterly period ended July 4, 2009 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 Company's Form 10-Q for the quarterly period ended July 4, 2009 fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Thomas F. Moynihan

Thomas F. Moynihan
Vice President, Finance

Dated: August 14, 2009