EMERGING VISION INC
Form 10-Q
August 16, 2010

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

FORM 10-Q

(Mark one)
[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended June 30, 2010

OR

[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _____________ to _____________

Commission file number: 1-14128

EMERGING VISION, INC.
(Exact name of Registrant as specified in its charter)

NEW YORK
(State or other jurisdiction of incorporation or organization)

11-3096941
(I.R.S. Employer Identification No.)

520 Eighth Avenue, 23rd Floor
New York, NY 10018
(Address and zip code of principal executive offices)

Registrant’s telephone number, including area code: (646) 737-1500

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

Yes X   No _

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

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

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

Yes No X

As of August 16, 2010, there were 125,292,806 outstanding shares of the Issuer's Common Stock, par value $0.01 per share.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

EMERGING VISION, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEETS
(In Thousands, Except Share Data)

ASSETS	June 30, 2010 (unaudited)	December 31, 2009
Current assets:		
Cash and cash equivalents	$1,349	$1,576
Franchise receivables, net of allowance of $179 and $188, respectively	1,849	1,665
Optical purchasing group receivables, net of allowance of $154 and $155, respectively	6,166	4,594
Other receivables, net of allowance of $47 and $15, respectively	291	237
Current portion of franchise notes receivable, net of allowance of $42	242	221
Inventories, net	342	309
Prepaid expenses and other current assets	376	447
Deferred tax assets	171	276
Total current assets	10,786	9,325
Property and equipment, net	779	872
Franchise notes receivable	366	290
Deferred tax asset, net of current portion	614	534
Goodwill	3,651	3,651
Intangible assets, net	2,747	2,839
Other assets	272	238
Total assets	$19,215	$17,749

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Accounts payable and accrued liabilities	$4,530	$4,564
Optical purchasing group payables	5,703	4,336
Put option liability – related party	700	700

Short-term debt	4,122	1,116
Related party obligations	338	334
Total current liabilities	15,393	11,050
Long-term debt	27	3,792
Related party borrowings, net of current portion	25	83
Franchise deposits and other liabilities	280	262
Total liabilities	15,725	15,187
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, $0.01 par value per share; 5,000,000 shares authorized: Senior Convertible Preferred Stock, $100,000 liquidation preference per share; 0.74 shares issued and outstanding	74	74
Common stock, $0.01 par value per share; 150,000,000 shares authorized; 125,475,143 and 128,992,938 shares issued, respectively, and 125,292,806 and 128,810,601 shares outstanding, respectively	1,254	1,289
Additional paid-in capital	128,059	128,024
Accumulated comprehensive loss	(328)	(150)
Accumulated deficit	(125,365)	(126,471)
Treasury stock, at cost, 182,337 shares	(204)	(204)
Total shareholders' equity	3,490	2,562
Total liabilities and shareholders' equity	$19,215	$17,749

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

EMERGING VISION, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME (LOSS)
(Unaudited) (In Thousands, Except Per Share Data)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2010	2009	2010	2009
Revenues:		< 10pt; color: #000000; background: transparent">	limit the right of stockholders to fill vacancies on the board of directors;	

limit the right of stockholders to act by written consent and to call a special meeting of stockholders or propose other actions;

require a higher percentage of stockholders than would otherwise be required to amend, alter, change or repeal our bylaws and certain provisions of our certificate of incorporation; and

authorize the issuance of preferred stock with any voting rights, dividend rights, conversion privileges, redemption rights and liquidation rights and other rights, preferences, privileges, powers, qualifications, limitations or restrictions as may be specified by our board of directors.

These provisions may:

discourage, delay or prevent a change in the control of our company or a change in our management, even if such change may be in the best interests of our stockholders;

adversely affect the voting power of holders of common stock; and

limit the price that investors might be willing to pay in the future for shares of our common stock.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

Stores

As of December 30, 2006, we operated 233 retail stores located primarily in major malls throughout the United States and Canada and 38 stores located in the United Kingdom and Ireland. Our mall-based stores generally range in size from 2,000 to 4,000 square feet and average approximately 2,800 square feet, while our tourist location stores currently range up to 6,000 square feet and our flagship store in New York City is approximately 20,000 square feet. Our stores are designed to be open and inviting for guests of all ages with an entryway that spans the majority of our storefront with wide aisles to accommodate families or groups. Our typical store has an oversized sentry bear at the front entry and features two stuffing machines, five NameMe computer stations, display units and flooring to enhance the guest traffic flow through the store. We select malls and make site selections within the mall based upon demographic analysis, market research, site visits and mall dynamics as well as a forecasting model that projects a potential location s first year sales. We have identified a significant number of target sites that meet our criteria for new stores in malls and tourist locations. We seek to locate our mall-based stores near major customer entrances to or in the center of malls and adjacent to other children, teen and family retailers. After we approve a site, it typically takes approximately 25 weeks to finalize the lease, design the layout, build out the site, hire and train associates, and stock the store for opening.

We lease all of our store locations. Due to our attraction as a family-oriented entertainment destination concept with average net sales per gross square foot that, in fiscal 2006, generally exceeded the average for the malls in which we operated, we have received numerous requests from mall owners and developers to locate a Build-A-Bear Workshop store in their malls. We believe that we generally have negotiated favorable exclusivity provisions in our leases.

Most of our leases have an initial term of ten years. A number of our leases provide a lease termination or kick out option to either party in a pre-determined year or years, typically the third or fourth year of the lease, if we do not meet certain agreed upon minimum sales levels. In addition, our leases typically require us to pay personal property taxes, our pro rata share of real property taxes of the shopping mall, our own utilities, repairs and maintenance in our store, a pro rata share of the malls common area maintenance and, in some instances, merchant association fees and media fund contributions. Most of our leases also require the payment of a fixed minimum rent as well as percentage rent based on sales in excess of agreed upon minimum annual sales levels.

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Following is a list of our 271 company-owned stores in the United States, Canada, the United Kingdom and Ireland as of December 30, 2006:

State	Number of Stores
Alabama	2
Arizona	4
Arkansas	3
California	23
Colorado	6
Connecticut	5
Delaware	1
Florida	12
Georgia	7
Hawaii	1
Idaho	1
Illinois	7
Indiana	6
Iowa	3
Kansas	2
Kentucky	3
Louisiana	3
Maine	1
Maryland	4
Massachusetts	9
Michigan	4
Minnesota	2
Mississippi	1
Missouri	6
Nebraska	1
Nevada	3
New Hampshire	2
New Jersey	12
New Mexico	1
New York	12
North Carolina	7
Ohio	10
Oklahoma	2
Oregon	3
Pennsylvania	8
Rhode Island	1
South Carolina	3
Tennessee	6
Texas	16
Utah	3
Virginia	6
Washington	4
West Virginia	1
Wisconsin	3

Canadian Province	
Alberta	2
British Columbia	2
Manitoba	1
Nova Scotia	1
Ontario	7
United Kingdom	
England	32
Scotland	4
Wales	1
Ireland	1

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Non-Store Properties

In addition to leasing all of our store locations, we lease approximately 52,000 square feet for our web fulfillment site and corporate headquarters, or World Bearquarters, in St. Louis, Missouri. Our World Bearquarters houses our corporate staff, our call center and our on-site training facilities. The lease commenced on January 1, 2005 with a four-year term, and may be extended for two additional five-year terms. In 2007, our web fulfillment site will be moving to our company-owned warehouse and distribution center.

In the United Kingdom, we lease approximately 2,000 square feet for our regional headquarters, or U.K. Bearquarters, in Windsor, England. The lease commenced on August 2003. The lease can be terminated at any time by either party giving notice of termination six months prior to cancellation.

In September 2006, we completed construction of a company-owned warehouse and distribution center, or Bearhouse, in Groveport, Ohio. The facility is approximately 350,000 square feet.

ITEM 3. LEGAL PROCEEDINGS

From time to time we are involved in ordinary routine litigation common to companies engaged in our line of business. We are involved in several court actions seeking to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. As of the date of this annual report on Form 10-K, we are not involved in any pending legal proceedings that we believe would be likely to have a material adverse effect on our financial condition or results of operations.

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

There were no matters submitted to a vote of security holders in the fourth quarter of fiscal 2006.

PART II

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

Our common stock is listed on the New York Stock Exchange (NYSE) under the symbol BBW. Our common stock commenced trading on the NYSE on October 28, 2004. The following table sets forth the high and low closing sale prices of our common stock for the periods indicated.

	Fiscal 2006		Fiscal 2005	
	High	Low	High	Low
First Quarter	$32.35	$26.89	$36.90	$29.44
Second Quarter	$32.30	$21.31	$31.08	$20.31
Third Quarter	$24.12	$19.79	$24.49	$19.86
Fourth Quarter	$32.00	$22.00	$31.97	$21.44

As of March 9, 2007, there were approximately 930 holders of record of the Company s common stock.

PERFORMANCE GRAPH

The following performance graph compares the 14-month cumulative total stockholder return of the Company s common Stock, with the cumulative total return on the Russell 2000® Index and an SEC-defined peer group of companies identified as SIC Code 5600-5699 (the Peer Group). The Peer Group consists of companies whose primary business is the operation of apparel and accessory retail stores. Build-A-Bear Workshop is not strictly a merchandise retailer and there is a strong interactive, entertainment component to the Company s business which differentiates it from retailers in the Peer Group. However, in the absence of any other readily identifiable peer group, we believe the use of the Peer Group is appropriate.

The performance graph starts with the Company s initial public offering on October 28, 2004 and ends on December 29, 2006, the last trading day prior to December 30, 2006, the end of the Company s fiscal 2006. The graph assumes that $100 was invested on October 28, 2004 in each of the Company s common stock, the Russell 2000® Index and the Peer Group, and that all dividends were reinvested.

These indices are included only for comparative purposes as required by Securities and Exchange Commission rules and do not necessarily reflect management s opinion that such indices are an appropriate measure of the relative performance of the Common Stock. They are not intended to forecast the possible future performance of the Common Stock.

Stock Repurchase Program

On February 20, 2007, we announced a $25 million share repurchase program of our outstanding common stock over the next twelve months. The program was authorized by our board of directors. Purchases may be made in the open market or in privately negotiated transactions, with the level and timing of activity depending on market conditions, other investment opportunities, and other factors. Purchases may be increased, decreased or discontinued at any time without notice. As of March 9, 2007, approximately 160,000 shares at an average price of $26.48 per share have been repurchased under this program. Future repurchases will be reported in our quarterly and annual reports under Item 5 on a monthly basis.

Recent Sales of Unregistered Securities

There were no sales of unregistered securities during the fourth quarter of fiscal 2006.

Dividend Policy

We paid a special $10.0 million cash dividend to our stockholders in August 2004. We anticipate that we will retain any future earnings to support operations and to finance the growth and development of our business, and we do not expect, at this time, to pay cash dividends in the future. Any future determination relating to our dividend policy will be made at the discretion of our board of directors and will depend on a number of factors, including future earnings, capital requirements, financial conditions, future prospects and other factors that the board of directors may deem relevant. Additionally, under our credit agreement, we are prohibited from declaring dividends without the prior consent of our lender, subject to certain exceptions, as described in Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

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ITEM 6. SELECTED FINANCIAL DATA

Throughout this annual report on Form 10-K, we refer to our fiscal years ended December 30, 2006, December 31, 2005, January 1, 2005, January 3, 2004, and December 28, 2002 as fiscal years 2006, 2005, 2004, 2003, and 2002, respectively. Our fiscal year consists of 52 or 53 weeks, and ends on the Saturday nearest December 31 in each year. Fiscal years 2006, 2005, 2004, and 2002 included 52 weeks and fiscal year 2003 included 53 weeks. All of our fiscal quarters presented in this annual report on Form 10-K included 13 weeks. When we refer to our fiscal quarters, or any three month period ending as of a specified date, we are referring to the 13-week period prior to that date.

The following table sets forth, for the periods and dates indicated, our selected consolidated financial and operating data. The balance sheet data as of December 30, 2006 and December 31, 2005 and the statement of operations and other financial data for our fiscal years ended December 30, 2006, December 31, 2005, and January 1, 2005 are derived from our audited financial statements included elsewhere in this annual report on Form 10-K. The balance sheet data as of January 1, 2005, January 3, 2004, and December 28, 2002 and the statement of operations and other financial data for our fiscal years ended January 3, 2004 and December 28, 2002 are derived from our audited financial statements that are not included in this annual report on Form 10-K. You should read our selected consolidated financial and operating data in conjunction with our consolidated financial statements and related notes and with Management s Discussion and Analysis of Financial Condition and Results of Operations appearing elsewhere in this annual report on Form 10-K.

See the notes to our consolidated financial statements for an explanation of the method used to determine the numbers of shares used in computing basic and diluted net earnings per common share.

	Fiscal Year				
	2006	**2005**	**2004**	**2003**	**2002**
	(Dollars in thousands, except share, per share and per gross square foot data)				
Statement of operations data:					
Total revenues	$ 437,072	$ 361,809	$ 301,662	$ 213,672	$ 169,138
Costs and expenses:					
Cost of merchandise sold	227,509	180,373	150,903	115,845	90,215
Selling, general and administrative	158,712	133,921	115,939	81,533	66,068
Store preopening	3,958	4,812	2,186	3,859	3,949
Interest expense (income), net	(1,530)	(1,710)	(299)	(58)	(88)
Total costs and expenses	388,649	317,396	268,729	201,179	160,144
Income before income taxes	48,423	44,413	32,933	12,493	8,994
Income tax expense	18,933	17,099	12,934	4,875	3,557
Net income	29,490	27,314	19,999	7,618	5,437
Cumulative dividends and accretion of redeemable preferred stock			1,262	1,970	1,971
Cumulative dividends on nonredeemable preferred stock			263	455	455
Net income available to common and participating preferred stockholders	$ 29,490	$ 27,314	$ 18,474	$ 5,193	$ 3,011

Net income allocated to common stockholders	$ 29,490	$ 27,314	$ 8,519	$ 116	$ 67
Net income allocated to participating preferred stockholders	$	$	$ 9,955	$ 5,077	$ 2,944
Earnings per common share:					
Basic	$ 1.46	$ 1.38	$ 2.30	$ 0.53	$ 0.31
Diluted	$ 1.44	$ 1.35	$ 1.07	$ 0.43	$ 0.29
Shares used in computing common per share amounts:					
Basic	20,169,814	19,735,067	3,702,365	217,519	217,519
Diluted	20,468,256	20,229,978	18,616,435	17,546,348	12,055,458

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	Fiscal Year				
	2006	2005	2004	2003	2002
	(Dollars in thousands, except share, per share and per gross square foot data)				
Other financial data:					
Gross margin ($) (1)	$ 205,063	$ 178,528	$ 149,566	$ 97,582	$ 78,908
Gross margin (%) (1)	47.4%	49.7%	49.8%	45.7%	46.7%
Capital expenditures (2)	$ 52,577	$ 31,083	$ 16,494	$ 24,917	$ 24,017
Depreciation and amortization	22,394	17,592	14,948	12,840	8,990
Cash flow data:					
Cash flows provided by operating activities	$ 53,035	$ 54,642	$ 48,527	$ 31,770	$ 23,963
Cash flows used in investing activities	(93,772)	(37,077)	(17,732)	(27,035)	(25,531)
Cash flows provided by (used in) financing activities	3,537	6,058	15,931		(121)
Cash dividends declared per common share	$	$	$ 0.55	$	$
Store data (3):					
Number of stores at end of period					
North America	233	200	170	150	108
United Kingdom and Ireland	38				
Total Stores	271	200	170	150	108
Square footage at end of period					
North America	712,299	615,194	514,341	461,982	344,503
United Kingdom and Ireland (4)	56,701				
Total square footage	769,000	615,194	514,341	461,982	344,503
Average net retail sales per store (5) (6)	$ 1,761	$ 1,864	$ 1,857	$ 1,605	$ 1,904
Net retail sales per gross square foot (6) (7)	$ 573	$ 615	$ 602	$ 502	$ 582
Comparable store sales change (%) (8)	(6.5)%	(0.2)%	18.1%	(15.9)%	(9.7)%
Balance sheet data:					
Cash and cash equivalents	$ 53,109	$ 90,950	$ 67,327	$ 20,601	$ 15,866
Working capital	27,952	66,646	48,000	10,463	7,376
Total assets	299,770	246,108	189,237	128,210	105,893
Redeemable preferred stock				37,890	35,920
Total stockholders equity	164,263	130,357	95,510	19,845	14,192

(1) Gross margin represents net

retail sales less cost of merchandise sold. Gross margin percentage represents gross margin divided by net retail sales.

(2) Capital expenditures consist of leasehold improvements, furniture and fixtures and computer equipment and software purchases.

(3) Excludes our webstore and seasonal and event-based locations.

(4) Square footage in the United Kingdom and Ireland is estimated selling square footage.

(5) Average net retail sales per store represents net retail sales from stores open throughout the entire period divided by the total number of such stores.

(6) When we refer to average net retail sales per

store and net retail sales per gross square foot for any period, we include in those calculations only those stores that have been open for that entire period.

(7) Net retail sales per gross square foot represents net retail sales from stores open throughout the entire period divided by the total gross square footage of such stores.

(8) Comparable store sales percentage changes are based on net retail sales and stores are considered comparable beginning in their thirteenth full month of operation.

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

The following Management s Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from the results discussed in the forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in Risk Factors and elsewhere in this annual report on Form 10-K. The following section is qualified in its entirety by the more detailed information, including our financial statements and the notes thereto, which appears elsewhere in this annual report on Form 10-K.

Overview

We are the leading, and only international, company providing a make your own stuffed animal interactive entertainment experience under the Build-A-Bear Workshop brand, in which our guests stuff, fluff, dress, accessorize and name their own teddy bears and other stuffed animals. Our concept, which we developed for mall-based retailing, capitalizes on what we believe is the relatively untapped demand for experience-based shopping as well as the widespread appeal of stuffed animals. The Build-A-Bear Workshop experience appeals to a broad range of age groups and demographics, including children, teens, their parents and grandparents. As of December 30, 2006, we operated 233 stores in the United States and Canada, 38 stores in the United Kingdom and Ireland, and had 34 franchised stores operating in international locations under the Build-A-Bear Workshop brand. In addition to our stores, we market our products and build our brand through our website, which simulates our interactive shopping experience, as well as our non-traditional store locations in Major League Baseball® ballparks, a location in a zoo, and our presence at event-based locations through our mobile store.

On April 2, 2006, we acquired all of the outstanding shares of The Bear Factory Limited, a stuffed animal retailer in the United Kingdom, and Amsbra Limited, our former U.K. franchisee. The results of this acquisition s operations have been included in the consolidated financial statements since that date. In conjunction with those transactions, we obtained 40 retail locations in the United Kingdom and Ireland. Four of those locations closed during 2006. Of those four locations, two closed due to overlapping store locations in the Amsbra and Bear Factory portfolios, and the other two locations are concessions within department stores, which is a format that we have chosen not to continue at this point in the United Kingdom. We converted and rebranded 25 Bear Factory stores to Build-A-Bear Workshop stores in time for the 2006 holiday season, resulting in a unified company brand throughout the U.K. and Ireland. During the store conversion and rebranding process, stores were temporarily closed on average for 22 days while many of the costs to operate the stores continue. Therefore, the acquisition was dilutive to earnings during fiscal 2006. The Company hopes to improve sales performance and adopt best practices in the areas of merchandising, marketing, purchasing and store operations, across the acquired store base, and to realize earnings accretion from the acquisition in fiscal 2007.

We operate in three segments that share the same infrastructure, including management, systems, merchandising and marketing, and generate revenues as follows:

- Company-owned retail stores located in the United States, Canada, the United Kingdom and Ireland, a webstore and seasonal, event-based locations;

- International stores operated under franchise agreements; and

- License arrangements with third parties which manufacture and sell to other retailers merchandise carrying the Build-A-Bear Workshop brand.

Selected financial data attributable to each segment for fiscal 2006, 2005, and 2004 are set forth in note 18 to our consolidated financial statements included elsewhere in this annual report on Form 10-K.

For a discussion of the key trends and uncertainties that have affected our revenues, income and liquidity, see the Revenues, Costs and Expenses and Expansion and Growth Potential subsections of this Overview.

We believe that we have developed an appealing retail store concept that, for stores open for the entire year, averaged $1.8 million in fiscal 2006 and $1.9 million in both fiscal 2005 and fiscal 2004 in net retail sales per store. For a discussion of the changes in comparable store sales in fiscal years 2006, 2005 and 2004, see Revenues. Store contribution, which consists of income before income tax expense, interest, store depreciation and amortization, store preopening expense and general and administrative expense, excluding franchise fees, income from licensing activities and contribution from our webstore and seasonal event-based locations, as a percentage of net retail sales, excluding revenue from our webstore and seasonal and event-based locations, was 24.7% for 2006 and 26.8% for fiscal 2005, and total company net income as a percentage of total revenues was 6.8% for fiscal 2006, and 7.5% for fiscal 2005. See Non-GAAP Financial Measures for a reconciliation of store contribution to net income. The store contribution of our

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average store, coupled with the fact that we have opened 198 stores in the United States and Canada since the beginning of fiscal 2001 have been the primary reasons for our net income increasing during each of the last five fiscal years. Additionally, as we have added stores and grown our sales volume, the quantities of merchandise and supplies we purchase have increased which has created economies of scale for our vendors allowing us to obtain reduced costs for these items and increase our profitability.

The increase in total store contribution has been partially offset by the increase in our central office general and administrative expenses required to support an expanding store base and international franchise operations. These expenses have grown at a slower rate, in percentage terms, than our number of stores and net retail sales.

We expect to grow our business primarily through the continued opening of new stores. Further, we expect to increase our net retail sales, including comparable store sales, as a result of the continuation of national television and online advertising which we added to our marketing mix in fiscal 2004. We also plan to increase our revenues through increasing the number of international franchised stores, as well as the addition of new licensees and sales of licensed products for which we receive license revenue.

We expect to realize leverage on our national advertising programs as we expand and open stores in new markets. We have been running national advertising since 2004 and believe that our brand awareness is higher and our entry into new markets is stronger as a result of the advertising and we expect to leverage these programs on an ongoing basis. We expect to improve our store productivity as a result of comparable store sales improvement and thereby improve our store contribution as a percentage of net retail sales by better leveraging our store level operating expenses, primarily those which are fixed such as occupancy, over increased net retail sales per store. As we grow our total revenues, we also expect to decrease our general and administrative expenses as a percentage of revenues by leveraging these expenses, primarily those which are largely fixed such as management payroll and occupancy, over an increased revenue amount. This decrease will be partially offset by some increases in general and administrative expenses, including marketing such as direct mail to support more stores and our growing international franchise business.

Following is a description and discussion of the major components of our statement of operations:

Revenues

Net retail sales: Net retail sales are revenues from retail sales (including our webstore and seasonal and event-based locations), are net of discounts, exclude sales tax, include shipping and handling costs billed to customers, and are recognized at the time of sale. Revenues from gift cards are recognized at the time of redemption. Our guests use cash, checks and third party credit cards to make purchases. We classify stores as new or comparable stores and do not include our webstore or seasonal, event-based locations in our store count or in our comparable store calculations. Stores enter the comparable store calculation in their thirteenth full month of operation. We opened four additional Friends 2B Made locations in 2006 to bring the total number of Friends 2B Made locations to nine as of December 30, 2006. All but one of these locations are within or adjacent to a Build-A-Bear Workshop store and share common store management, employees and infrastructure. Other than our stand-alone store in Ontario, California, these locations are considered expansions of the existing Build-A-Bear Workshop store and are not considered an addition to our total store count. The net retail sales of these expanded Build-A-Bear Workshop stores are excluded from comparable store sales calculations until the thirteenth full month of operation after the date of the expansion.

We have an automated frequent shopper program in the United States, the Stuff Fur Stuff® club, whereby guests enroll in the program and receive one point for every dollar or partial dollar spent and after reaching 100 points receive a $10 discount on a future purchase. This program was automated in July 2006 and replaced our former Buy Stuff Program, which was a manual punch card system with limited tracking capability. The reward earned under the new program did not change. An estimate of the obligation related to the program, based on historical redemption rates, is recorded as deferred revenue and a reduction of net retail sales at the time of purchase. The deferred revenue obligation is reduced, and a corresponding amount is recognized in net retail sales, in the amount of and at the time of redemption of the $10 discount. We account for changes in the deferred revenue account at the total company level only. This is due to the fact that the frequent buyer discount can be earned or redeemed at any of our store locations. Therefore, when we refer to net retail sales by location, such as comparable stores or new stores, these amounts do not include any changes in the deferred revenue amount. See Critical Accounting Policies for additional details on the accounting for the deferred revenue program.

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We use net retail sales per gross square foot and comparable store sales as performance measures for our business. The following table details net retail sales per gross square foot by age of store for the periods presented:

	Fiscal 2006	Fiscal 2005	Fiscal 2004
Net retail sales per gross square foot (1) (2)			
Store Age > 5 years (66 stores in 2006, 34 stores in 2005, 13 stores in 2004)	$577	$623	$691
Store Age 3-5 years (80 stores in 2006, 69 stores in 2005, 55 stores in 2004)	$556	$593	$576
Store Age < 3 years (54 stores in 2006, 66 stores in 2005, 79 stores in 2004)	$592	$637	$608
All comparable stores	$573	$615	$602

(1) Net retail sales per gross square foot represents net retail sales from stores open throughout the entire period divided by the total gross square footage of such stores. As such, stores in the UK are excluded from the calculation. Calculated on an annual basis only.

(2) Excludes our webstore and seasonal and event-based locations.

The percentage increase (or decrease) in comparable store sales for the periods presented below is as follows:

	Fiscal 2006	Fiscal 2005	Fiscal 2004
Comparable store sales change (%) (1) (2)			
Store Age > 5 years (66 stores in 2006, 34 stores in 2005, 13 stores in 2004)	(5.2)%	4.0%	24.0%
Store Age 3-5 years (80 stores in 2006, 69 stores in 2005, 55 stores in 2004)	(6.3)%	(0.2)%	19.7%
Store Age < 3 years (54 stores in 2006, 66 stores in 2005, 79 stores in 2004)	(9.4)%	(3.3)%	15.1%

Total comparable store sales change	(6.5)%	(0.2)%	18.1%

(1) Comparable store sales percentage changes are based on net retail sales and stores are considered comparable beginning in their thirteenth full month of operation.

(2) Excludes our webstore and seasonal and event-based locations.

Our net retail sales per gross square foot are among the highest for specialty retailers. Historically, as a group our younger stores have performed at the highest sales per square foot level, above the chain-wide average, despite experiencing comparable store sales pressures. Often our stores open with strong sales performance in their first year of operation and show comparable store sales declines in years two and three. Our older stores consistently perform the best on a comparable store sales basis and younger stores consistently generate the highest sales per square foot. New stores typically pay for themselves in their first year of operation.

Comparable store sales decreased by 6.5% in fiscal 2006 following a decrease of 0.2% in fiscal 2005. We believe these changes can be attributed primarily to the following factors:

Changing customer preferences in 2006 contributed to the decline in comparable store sales. Our repeat customers, many of whom have built a sizable collection of Build-A-Bear Workshop stuffed animals, have become more product discriminating. Additionally, in the fourth quarter of 2006, inventory shortfalls on products, specifically our special holiday animal Mumble, impacted store performance. Demand was greater than we had anticipated and coupled with our customer s changing preferences contributed to a fourth quarter negative comparable store sales decrease of 10.4%.

In 2006, we saw improvement in our average transaction value per guest. However, there was a decline in customer traffic during fiscal 2006 compared to 2005.

Due to the discretionary nature of our products, we believe that during much of 2006 comparable store sales were impacted by the more difficult macro economic conditions generally impacting customers.

Comparable store sales decreased by 0.2% in fiscal 2005 following an increase of 18.1% in fiscal 2004. We believe these changes can be attributed primarily to the following factors:

Our ongoing programs in advertising. During the fourth quarter of fiscal 2003, we tested in a limited number of markets the use of television and online advertising and determined that it was successful in attracting a higher number of new and repeat guests. In the first quarter of fiscal 2004, we implemented this marketing strategy on a national basis and quickly began achieving

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comparable store sales increases. We continued this marketing approach throughout fiscal 2005. This approach was successful in maintaining our comparable store sales levels, but did not produce the increases that were achieved in fiscal 2004 when the change in the marketing program was an incremental addition to the prior year.

Following an improved economy in 2004, with higher levels of consumer confidence and a better retail climate, the economy showed mixed results in 2005 with varying levels of consumer confidence, record levels of crude oil prices and significant weather activity, particularly during the hurricane season.

Franchise fees: We receive an initial, one-time franchise fee for each master franchise agreement which is amortized to revenue over the life of the respective franchise agreement, which extend for periods up to 10 years.

Master franchise rights are typically granted to a franchisee for an entire country or countries. Continuing franchise fees are based on a percentage of sales made by the franchisees stores and are recognized as revenue at the time of those sales.

As of December 30, 2006, we had 34 stores, including 15 opened in fiscal 2006, operating under franchise arrangements in the following countries:

Japan	7
Australia	6
Denmark	5
Taiwan	3
Other	13

On April 2, 2006, we acquired all of the outstanding shares Amsbra Limited, our former U.K. franchisee. Amsbra operated all 11 of the franchised Build-A-Bear Workshop stores located in the United Kingdom. Upon completion of the acquisition, all of the franchised locations in the United Kingdom became company-owned stores.

Licensing revenue: Licensing revenue is based on a percentage of sales made by licensees to third parties and is recognized at the time the product is shipped by the licensee or at the point of sale. We have entered into a number of licensing arrangements whereby third parties manufacture and sell to other retailers merchandise carrying the Build-A-Bear Workshop trademark.

Costs and Expenses

Cost of merchandise sold and gross margin: Cost of merchandise sold includes the cost of the merchandise, royalties paid to licensors of third party branded merchandise, store occupancy cost, including store depreciation, freight costs from the manufacturer to the store, cost of warehousing and distribution, packaging, damages and shortages, and shipping and handling costs incurred in shipment to customers. Gross margin is defined as net retail sales less the cost of merchandise sold.

We have been able to reduce the unit costs of our merchandise and packaging through economies of scale realized as our sales volume has grown. The increase in sales volume has also allowed us to reduce our freight, cost of warehousing and distribution costs as a percentage of net retail sales as a result of the cost efficiencies of shipping higher volumes of merchandise. We expect to maintain these efficiencies in the future.

Selling, general and administrative expense: These expenses include store payroll and benefits, advertising, credit card fees, and store supplies, as well as central office general and administrative expenses, including management payroll, benefits, stock-based compensation, travel, information systems, accounting, insurance, legal and public relations. These expenses also include depreciation and amortization of central office leasehold improvements, furniture, fixtures and equipment as well as the amortization of intellectual property costs.

Central office general and administrative expenses have grown over time in order to support the increased number of stores in operation and we believe will continue to grow as we add stores, but we expect this increase to be at a lower rate than the percentage increase in total revenues. Advertising increased significantly with the introduction in fiscal 2004 of our national television and online advertising campaign. We maintained the level of advertising expense as a percentage of net retail sales in fiscal 2006 as compared to fiscal 2005 and fiscal 2004, and anticipate continuing this level of advertising expenditures in the future. Other store expenses such as credit card fees and supplies historically have increased or decreased proportionately with net retail sales.

We granted options during fiscal 2004 at an exercise price of $8.78 per share, which had been determined to be the fair value of our common stock at the time based on an independent appraisal. Subsequent to such grants, we determined that the fair value of the underlying common stock should have been deemed to be approximately $15.00 per share. As a result of this determination, this option issuance generated stock-based compensation of $1.9 million to be recognized over the vesting period of the 302,234 underlying options issued. These options became fully vested upon the completion of our initial public offering on October 28, 2004. Accordingly, all unrecognized compensation expense related to this grant was recognized at that time and is reflected in the consolidated statement of operations for fiscal 2004 as a component of selling, general and administrative expense.

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On January 1, 2006, we adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R). The provisions of SFAS 123R require that all share-based payments to employees be recognized in the financial statements based on the fair value of the instruments issued. SFAS 123R requires the recognition of compensation expense related to instruments issued following adoption as well as to the non-vested portion of instruments issued prior to adoption of the standard. After the adoption of SFAS 123R, we anticipate that our share-based employee compensation will primarily consist of the granting of non-vested stock which vests over a pre-determined period of time assuming continued employment. In the past, our share-based employee compensation consisted primarily of stock option awards which vested over a pre-determined period of time assuming continued employment. In 2006 we recorded stock-based compensation of approximately $2.1 million ($1.4 million net of taxes) in fiscal 2006 following the adoption of SFAS 123R. Of this amount, $0.2 million ($0.2 after tax) is attributable to the Company s adoption of SFAS 123R. This incremental expense from the adoption of SFAS 123R did not reduce basic or diluted earnings per share based upon the insignificance of the expense. The additional stock-based compensation expense not related to the adoption of SFAS 123R was related to the vesting of restricted stock awards. In 2005, we recorded stock based compensation of approximately $0.8 million ($0.5 million net of tax).

Store preopening: Preopening costs are expensed as incurred and include store set-up, certain labor and hiring costs, and rental charges incurred prior to a store s opening.

Expansion and Growth Potential

Company-Owned Stores:

The number of Build-A-Bear Workshop stores in the United States, Canada, United Kingdom, and Ireland for the last three fiscal years can be summarized as follows:

	Fiscal 2006	Fiscal 2005	Fiscal 2004
Beginning of period	200	170	150
U.K. Acquisition	40		
Opened	35	30	21
Closed	(4)		(1)
End of period	271	200	170

On April 2, 2006 the Company acquired all of the outstanding shares of The Bear Factory Limited (Bear Factory), a stuffed animal retailer in the United Kingdom, and Amsbra Limited (Amsbra), the Company s former U.K. franchisee (collectively, the U.K. Acquisition). In conjunction with those transactions, we obtained 40 retail locations in the United Kingdom and Ireland. Four of those locations closed during 2006. Of those four locations, two closed due to overlapping store locations in the Amsbra and Bear Factory portfolios, and the other two locations are concessions within department stores, which is a format that we have chosen not to continue at this point in the United Kingdom. We opened two new store locations in the United Kingdom in fiscal 2006.

In fiscal 2007, we anticipate opening 37 Build-A-Bear Workshop stores in the United States and Canada and 7 to 10 stores in the United Kingdom and Ireland. We believe there is a market potential for at least 350 Build-A-Bear Workshop stores in the United States and Canada and 70 to 75 stores in the United Kingdom and Ireland. In fiscal 2003, we began testing in certain markets our initial brand expansion initiative, our proprietary Friends 2B Made line of make-your-own dolls and related products. In fiscal 2004, we opened two Friends 2B Made locations within or adjacent to existing Build-A-Bear Workshop stores. In fiscal 2005, we opened three additional locations in or adjacent to new or existing Build-A-Bear Workshop stores. In fiscal 2006, we opened three additional locations in or adjacent to new or existing Build-A-Bear Workshop stores and one stand alone Friends 2B Made store in Ontario, California. Other than the one stand alone store, the Friends 2B Made stores are not included in the number of store openings in fiscal 2006, 2005 or 2004 as noted above but rather are considered expansions of Build-A-Bear Workshop stores. The Friends 2B Made merchandise is also offered from a separate display fixture in select Build-A-Bear Workshop stores.

Non-Store Locations:

In 2004 we began offering merchandise in seasonal, event-based locations such as Major League Baseball® ballparks, as well as at temporary locations such as at the NBA All-Star Jam Session. We expect to expand our future presence at select seasonal, event-based locations contingent on their availability. As of the end of December 30, 2006 we had a total of five ballpark locations. We also opened up our first store in a zoo during fiscal 2006.

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International Franchise Revenue:

Our first franchisee location was opened in November 2003. The number of international, franchised stores opened and closed for the periods presented below can be summarized as follows:

	Fiscal 2006	Fiscal 2005	Fiscal 2004
Beginning of period	30	12	1
U.K. Acquisition	(11)		
Opened	15	18	12
Closed			(1)
End of period	34	30	12

As of December 30, 2006, we had 13 master franchise agreements, which typically grant franchise rights for a particular country or countries, covering 15 countries. We anticipate signing additional master franchise agreements in the future. We expect our current and future franchisees to open 20 to 25 stores in fiscal 2007. We believe there is a market potential for approximately 300 franchised stores outside of the United States, Canada, the United Kingdom, and Ireland.

In April 2006, we acquired Amsbra Limited, our former franchisee in the United Kingdom. Amsbra owned all 11 franchised Build-A-Bear Workshop stores in the United Kingdom. Upon completion of the transaction, all of the franchised locations in the United Kingdom became company-owned stores.

Licensing Revenue:

In fiscal 2004, we began entering into license agreements pursuant to which we receive royalties on Build-A-Bear Workshop brand products. These agreements generated revenue of approximately $1.0 million in 2006, $0.9 million in fiscal 2005, and $0.3 million in 2004. We anticipate entering into additional license agreements in the future.

Results of Operations

The following table sets forth, for the periods indicated, selected statement of operation data expressed as a percentage of total revenues, except where otherwise indicated. Percentages will not total due to cost of merchandise sold being expressed as a percentage of net retail sales and rounding:

	Fiscal 2006	Fiscal 2005	Fiscal 2004
Revenues:			
Net retail sales	99.0%	99.2%	99.6%
Franchise fees	0.8	0.5	0.3
Licensing revenues	0.2	0.3	0.1
Total revenues	100.0	100.0	100.0
Costs and expenses:			
Cost of merchandise sold (1)	52.6	50.3	50.2
Selling, general and administrative	36.3	37.0	38.4
Store preopening	0.9	1.3	0.7
Interest expense (income), net	(0.4)	(0.5)	(0.1)
Total costs and expenses	88.9	87.7	89.1
Income before income taxes	11.1	12.3	10.9
Income tax expense	4.3	4.7	4.3
Net income	6.8%	7.5%	6.6%

Gross margin (%)(2)	47.4%	49.7%	49.8%

(1) Cost of merchandise sold is expressed as a percentage of net retail sales.

(2) Gross margin represents net retail sales less cost of merchandise sold. Gross margin percentage represents gross margin divided by net retail sales.

Fiscal Year Ended December 30, 2006 (52 weeks) Compared to Fiscal Year Ended December 31, 2005 (52 weeks)

Total revenues. Net retail sales increased to $432.6 million for fiscal 2006 from $358.9 million for fiscal 2005, an increase of $73.7 million, or 20.5%. Sales from new stores contributed a $55.0 million increase in net retail sales. Sales from our acquisition of Amsbra and The Bear Factory contributed $32.7 million and sales from non-store locations and non-comparable stores resulted in a $3.0 million increase in net retail sales. Included in net retail sales in fiscal 2006 is an adjustment to deferred revenue of $3.6 million, effective at the beginning of fiscal 2006, related to the most recent assessment of redemption rates on our customer loyalty program. Offsetting these increases, comparable store sales decreased $22.2 million, or 6.5%.

Revenue from international franchise fees increased to $3.5 million for fiscal 2006 from $2.0 million for fiscal 2005, an increase of $1.5 million. This increase was primarily due to the addition of new franchisees and new franchised stores in fiscal 2006. Licensing revenue was $1.0 million in fiscal 2006 compared to $0.9 million in fiscal 2005.

Gross margin. Gross margin increased to $205.1 million for fiscal 2006 from $178.5 million for fiscal 2005, an increase of $26.6 million, or 14.9%. As a percentage of net retail sales, gross margin decreased to 47.4% for fiscal 2006 from 49.7% for fiscal 2005, a decrease of 2.3%. This decrease was anticipated and resulted primarily from higher occupancy costs as a percentage of net retail sales in the U.K. Higher occupancy costs in the U.S. and Canada as a percentage of net retail sales resulting from the decline in comparable store sales, and higher shipping and transportation costs primarily related to the transition to our company-owned distribution center, also contributed to the decline in gross margin as a percentage of net retail sales. Improved merchandise margins partially offset the decrease in gross margin percentage.

Selling, general and administrative. Selling, general and administrative expenses were $158.7 million for fiscal 2006 as compared to $133.9 million for fiscal 2005, an increase of $24.8 million, or 18.5%. As a percentage of total revenues, selling, general and administrative expenses decreased to 36.3% for fiscal 2006 as compared to 37.0% for fiscal 2005, a decrease of 0.7%. The dollar increase was primarily due to 71 more stores, which includes the acquired U.K. stores, in operation at December 30, 2006 as compared to December 31, 2005 with the increased salaries at the stores and central office to support the larger store base. Selling, general and administrative expense as a percentage of total revenues was lower primarily due to a reduction in the percentage of advertising expense as compared to total revenues, the leveraging of store payroll over a larger revenue base, and a decline in the central office management payroll resulting primarily from a reduction in performance-based bonus expense. These decreases were partially offset by increased stock-based compensation expense.

Store preopening. Store preopening expense was $4.0 million for fiscal 2006 as compared to $4.8 million for fiscal 2005. These amounts include preopening rent expense of $0.6 million in fiscal 2006 and $1.5 million in fiscal 2005. The decrease was primarily due to preopening costs of $1.8 million related to our flagship store and café in New York City. Offsetting the impact of the flagship store, five more new stores were opened in fiscal 2006 than in fiscal 2005 (35 in fiscal 2006, including two U.K. stores, as compared to 30 in fiscal 2005). Preopening expenses include expenses for stores that have opened as well as some expenses incurred for stores that will be opened at a later date.

Interest expense (income), net. Interest income, net of interest expense, was $1.5 million for fiscal 2006 as compared to $1.7 million for fiscal 2005. This decrease was the result of lower cash balances throughout fiscal 2006 due to capital expenditures for our distribution center and cash used for the acquisition of Amsbra and The Bear Factory.

Provision for income taxes. The provision for income taxes was $18.9 million for fiscal 2006 as compared to $17.1 million for fiscal 2005. The effective tax rate was 39.1% for fiscal 2006 and 38.5% for fiscal 2005. The increase in the effective tax rate was principally due to the impact of the U.K. acquisition and the inability to record a benefit for net operating losses generated by the U.K. operations in the current year.

Fiscal Year Ended December 31, 2005 (52 weeks) Compared to Fiscal Year Ended January 1, 2005 (52 weeks)

Total revenues. Net retail sales increased to $358.9 million for fiscal 2005 from $300.5 million for fiscal 2004, an increase of $58.4 million, or 19.4%. Sales from new stores contributed a $54.8 million increase in net retail sales. Sales over the Internet increased by $2.4 million, or 38.8%, and sales from non-store locations and non-comparable stores resulted in a $0.7 million increase in net retail sales. Comparable store sales decreased $0.5 million, or 0.2%.

Revenue deferrals under our frequent shopper program decreased to $1.6 million in fiscal 2005 compared to $2.6 million in fiscal 2004 and resulted in a $1.0 million increase in net retail sales.

Revenue from international franchise fees increased to $2.0 million for fiscal 2005 from $0.8 million for fiscal 2004, an increase of $1.2 million. This increase was primarily due to the addition of new franchisees and new franchised stores in fiscal 2005. Licensing revenue was $0.9 million in fiscal 2005 compared to $0.3 million in fiscal 2004.

Gross margin. Gross margin increased to $178.5 million for fiscal 2005 from $149.6 million for fiscal 2004, an increase of $28.9 million, or 19.3%. As a percentage of net retail sales, gross margin decreased to 49.7% for fiscal 2005 from 49.8% for fiscal

2004, a decrease of 0.1%. Higher shipping costs related to increased fuel surcharges accounted for 0.3% of the decrease in gross margin. Higher occupancy cost as a percentage of net retail sales, resulting from flat comparable store sales, accounted for 0.2% of this decrease. These decreases were partially offset by lower product and supply costs, as a percentage of net retail sales, resulting from purchasing cost efficiencies related to higher sales volumes, which accounted for a 0.3% increase in gross margin. Reduced inventory damages and shortages also offset the decrease in gross margin by 0.1%.

Selling, general and administrative. Selling, general and administrative expenses were $133.9 million for fiscal 2005 as compared to $115.9 million for fiscal 2004, an increase of $18.0 million, or 15.5%. As a percentage of total revenues, selling, general and administrative expenses decreased to 37.0% for fiscal 2005 as compared to 38.4% for fiscal 2004, a decrease of 1.4%. The dollar increase was primarily due to 30 more stores in operation at December 31, 2005 as compared to January 1, 2005. Selling, general and administrative expense as a percentage of total revenues was 1.5% lower due to the leveraging of central office and store payroll costs, primarily as a result of lower performance-based bonuses in 2005 as compared to 2004. Lower stock-based compensation also decreased selling, general and administrative expenses by 0.4% as a percentage of total revenues. These decreases were partially offset by higher legal, accounting and insurance costs primarily associated with being a public company for the entire period in fiscal 2005 which resulted in a 0.4% increase as a percentage of total revenues.

Store preopening. Store preopening expense was $4.8 million for fiscal 2005 as compared to $2.2 million for fiscal 2004. These amounts include preopening rent expense of $1.5 million in fiscal 2005 and $0.4 million in fiscal 2004. Approximately $2.0 million of this increase, including approximately $0.9 million of preopening rent expense, was due to the preopening costs related to our flagship store and café in New York City. Excluding our flagship store, eight more new stores were opened in fiscal 2005 than in fiscal 2004 (29 in fiscal 2005 as compared to 21 in fiscal 2004). Preopening expenses include expenses for stores that have opened as well as some expenses incurred for stores that will be opened at a later date.

Interest expense (income), net. Interest income, net of interest expense, was $1.7 million for fiscal 2005 as compared to $0.3 million for fiscal 2004. This increase was the result of higher cash balances throughout fiscal 2005.

Provision for income taxes. The provision for income taxes was $17.1 million for fiscal 2005 as compared to $12.9 million for fiscal 2004. The effective tax rate was 38.5% for fiscal 2005 and 39.3% for fiscal 2004. The decrease in the effective tax rate was principally due to non-deductible stock compensation charges incurred in fiscal 2004.

Non-GAAP Financial Measures

We use the term store contribution throughout this annual report on Form 10-K. Store contribution consists of income before income tax expense, interest, store depreciation and amortization, store preopening expense and general and administrative expense, excluding franchise fees, income from licensing activities and contribution from our webstore and seasonal and event-based locations. This term, as we define it, may not be comparable to similarly titled measures used by other companies and is not a measure of performance presented in accordance with U.S. generally accepted accounting principles (GAAP).

We use store contribution as a measure of our stores operating performance. Store contribution should not be considered a substitute for net income, net income per store, cash flows provided by operating activities, cash flows provided by operating activities per store, or other income or cash flow data prepared in accordance with GAAP.

We believe store contribution is useful to investors in evaluating our operating performance because it, along with the number of stores in operation, directly impacts our profitability. Historically, central office general and administrative expenses and preopening expenses have increased at a rate less than our total net retail sales increases. Therefore, as we have opened additional new stores and leveraged our central office general and administrative and preopening expenses over this larger store base and sales volume, we have been able to increase our net income each year.

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The following table sets forth a reconciliation of store contribution to net income for our company-owned stores located in the United States and Canada (North America), stores located the U.K. and Ireland (United Kingdom) and for our consolidated store base:

	Fiscal 2006			Fiscal 2005		
	North America	United Kingdom	Total	North America	United Kingdom	Total
Net income (1)	$ 30,942	$ (1,452)	$ 29,490	$ 27,314	$	$ 27,314
Income tax expense	18,933		18,933	17,099		17,099
Interest expense (income)	(1,530)		(1,530)	(1,710)		(1,710)
Store depreciation and amortization (2)	15,986	1,655	17,641	13,985		13,985
Store preopening expense	3,209	749	3,958	4,812		4,812
General and administrative expense (3)	38,596	2,010	40,606	34,000		34,000
Franchising and licensing contribution (4)	(2,409)	(90)	(2,499)	(1,107)		(1,107)
Non-store activity contribution (5)	(3,464)		(3,464)	(1,499)		(1,499)
Store contribution	$ 100,263	$ 2,872	$ 103,135	$ 92,894	$	$ 92,894
Total revenues	$ 404,109	$ 32,717	$ 436,826	$ 361,809	$	$ 361,809
Franchising and licensing revenues	(4,410)		(4,410)	(2,907)		(2,907)
Revenues from non-store activities (5)	(15,191)		(15,191)	(12,131)		(12,131)
Store location net retail sales	$ 384,508	$ 32,717	$ 417,225	$ 346,771	$	$ 346,771
Store contribution as a percentage of store location net retail sales	26.1%	8.8%	24.7%	26.8%	0.0%	26.8%
Total net income as a percentage of total revenues	7.7%	-4.4%	6.8%	7.5%	0.0%	7.5%

(1) Includes a change in estimate to deferred revenue related to our customer loyalty program of $2.2 million.

(2) Store depreciation and amortization includes depreciation and amortization of all capitalized assets in store locations, including leasehold

improvements, furniture and fixtures, and computer hardware and software.

(3) General and administrative expenses consist of non-store, central office general and administrative functions such as management payroll and related benefits, travel, information systems, accounting, purchasing and legal costs as well as the depreciation and amortization of central office leasehold improvements, furniture and fixtures, computer hardware and software and intellectual property. General and administrative expenses also include a central office marketing department, primarily payroll and related benefits expense, but exclude advertising expenses, such as direct mail catalogs and television

advertising, which are included in store contribution.

(4) Franchising and licensing contribution includes franchising and licensing revenues and all expenses attributable to the franchising and licensing segments other than depreciation, amortization and interest expense/income. Depreciation and amortization related to franchising and licensing is included in the general and administrative expense caption. Interest expense/income related to franchising and licensing is included in the interest expense (income) caption.

(5) Non-store activities include our webstore, seasonal and event-based locations and franchising and licensing activities.

Seasonality and Quarterly Results

The following is a summary of certain unaudited quarterly results of operations data for each of the last two fiscal years.

	Fiscal 2006				Fiscal 2005			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(Dollars in millions, except per share data)							
Total revenues	$98.6	$ 93.7	$ 101.5	$ 143.3	$86.1	$ 73.7	$ 84.0	$ 118.0
Gross margin(1)	47.9	40.8	42.4	74.0	43.3	34.5	40.0	60.8
Net income	8.4	3.0	2.7	15.4	8.0	3.5	5.3	10.6
Net income allocated to common stockholders	8.4	3.0	2.7	15.4	8.0	3.5	5.3	10.6
Earnings per common share:								
Basic	0.42	0.15	0.13	0.76	0.41	0.18	0.26	0.53
Diluted	0.41	0.15	0.13	0.75	0.40	0.17	0.26	0.52
Number of stores (end of quarter)	202	256	264	271	173	186	193	200

(1) Gross margin represents net retail sales less cost of merchandise sold.

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Our operating results for one period may not be indicative of results for other periods, and may fluctuate significantly because of a variety of factors, including those discussed under Risk Factors Fluctuations in our quarterly results of operations could cause the price of our common stock to substantially decline.

The timing of new store openings may result in fluctuations in quarterly results as a result of the revenues and expenses associated with each new store location. We typically incur most preopening costs for a new store in the three months immediately preceding the store s opening. We expect our growth, operating results and profitability to depend in some degree on our ability to increase our number of stores.

For accounting purposes, the quarters of each fiscal year consist of 13 weeks, although we will have a 14-week quarter approximately once every six years. Quarterly fluctuations and seasonality may cause our operating results to fall below the expectations of securities analysts and investors, which could cause our stock price to fall.

Liquidity and Capital Resources

Our cash requirements are primarily for the opening of new stores, information systems and working capital. Historically, we have met these requirements through capital generated from the sale and issuance of our securities to private investors and through our initial public offering, cash flow provided by operations and our revolving line of credit. From our inception to December 2001, we raised at various times a total of $44.9 million in capital from several private investors. In 2004, we raised $25.7 million from the initial public offering of our common stock. From fiscal 2002 to fiscal 2005, cash flows provided by operating activities have exceeded cash flows used in investing activities.

Operating Activities. Cash flows provided by operating activities were $53.0 million in fiscal 2006, $54.6 million in fiscal 2005 and $48.5 million in fiscal 2004. Cash flow from operating activities decreased in fiscal 2006 from fiscal 2005 primarily due to increased cash outflows for inventories offset by the timing of cash payments on accounts payable and accrued expenses. Additionally, the adoption of SFAS 123R led to the reclassification of the tax benefit from the exercise of stock options from operating activities to financing activities. This caused the impact of this line item on cash flows to decrease by $4.4 million. Cash flow from operating activities increased in fiscal 2005 from fiscal 2004 primarily due to increases in net income adjusted for the impact of depreciation and amortization.

Investing Activities. Cash flows used in investing activities were $93.8 million in fiscal 2006, $37.1 million in fiscal 2005 and $17.7 million in fiscal 2004. Cash used in investing activities during fiscal 2006 relates primarily to the U.K. acquisition for $39.1 million, the construction of our company-owned distribution center for approximately $22 million, and 35 new stores. Cash used in investing activities during fiscal 2005 and 2004 relates primarily to 30 new stores in fiscal 2005 and 21 in fiscal 2004. In fiscal 2005, a loan made to one of our franchisees used cash of $4.4 million. No loans were made in fiscal 2004.

Financing Activities. Cash flows provided by financing activities were $3.5 million in fiscal 2006, $6.1 million in fiscal 2005, and $15.9 million in fiscal 2004. In fiscal 2006, exercises of employee stock options and employee stock purchases and related tax benefits provided cash of $3.4 million, as compared to $4.4 million in fiscal 2005 and $0.1 million in fiscal 2004. The collection of a note receivable from an officer of the Company provided cash of $1.6 million in fiscal 2005. A similar note collection in fiscal 2004 provided cash of $0.1 million. In fiscal 2004, we completed our initial public offering which resulted in cash inflows, net of offering costs, of $25.7 million. The financing cash inflows from the initial public offering were partially offset by the payment of a special cash dividend in August 2004 of $10.0 million.

Capital Resources. As of December 30, 2006, we had a cash balance of $53.1 million. We also have a line of credit, which we can use to finance capital expenditures and seasonal working capital needs throughout the year. The credit agreement is with U.S. Bank, National Association and was amended effective June 30, 2006 to include a seasonal overline from July 1 to December 31 each year during which the line availability increases from $15 million to $30 million. Borrowings under the credit agreement are not collateralized, but availability under the credit agreement can be limited by the vendor based on our level of accounts receivable, inventory, and property and equipment. The credit agreement expires on September 30, 2007 and contains various restrictions on indebtedness, liens, guarantees, redemptions, mergers, acquisitions or sale of assets, loans, transactions with affiliates, and investments. It also prohibits us from declaring dividends without the bank s prior consent, unless such payment of dividends would not violate any terms of the loan agreement. Borrowings bear interest at our option of prime minus

1.0% or LIBOR plus 1.5%. Financial covenants include maintaining a minimum tangible net worth, maintaining a minimum fixed charge cover ratio (as defined in the credit agreement) and not exceeding a maximum funded debt to earnings before interest, depreciation and amortization ratio. As of December 30, 2006, we were in compliance with these covenants. There were no borrowings under our line of credit as of December 30, 2006. There was a standby letter of credit of approximately $1.1 million outstanding under the credit agreement as of December 30, 2006. Accordingly, there was approximately $28.9 million available for borrowing under the line of credit as of December 30, 2006.

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Most of our retail stores are located within shopping malls and all are operated under leases classified as operating leases. Our leases in North America typically have a ten-year term and contain provisions for base rent plus percentage rent based on defined sales levels. Many of the leases contain a provision whereby either we or the landlord may terminate the lease after a certain time, typically in the third to fourth year of the lease, if a certain minimum sales volume is not achieved. In addition, some of these leases contain various restrictions relating to change of control of our company. Our leases also subject us to risks relating to compliance with changing mall rules and the exercise of discretion by our landlords on various matters, including rights of termination in some cases.

Our leases in the U.K. typically have terms of 10-15 years and generally contain a provision whereby every fifth year the rental rate can be adjusted to reflect the current market rates. The leases typically provide the lessee with the first right for renewal at the end of the lease. We may also be required to make deposits and rent guarantees to secure new leases as we expand. Real estate taxes also change according to government time schedules to reflect current market rental rates for the locations we lease.

In fiscal 2007, we expect to spend a total of $35 to $40 million on capital expenditures. Capital spending in fiscal 2006 totaled $52.6 million. Capital spending in fiscal 2006 was primarily for the construction of our new distribution center, the opening of 35 new stores (33 in North America and two in the United Kingdom), the re-branding of 25 stores in the United Kingdom, and the continued installation and upgrades of central office information technology systems. In fiscal 2006, the average investment per new store, which includes leasehold improvements, fixtures, equipment and inventory, was approximately $0.5 million. We anticipate the investment per store in fiscal 2007 will be approximately the same as fiscal 2006.

On February 20, 2007, we announced a $25 million share repurchase program of our outstanding common stock over the next twelve months. The program was authorized by our board of directors. Purchases may be made in the open market or in privately negotiated transactions, with the level and timing of activity depending on market conditions, other investment opportunities, and other factors. Purchases may be increased, decreased or discontinued at any time without notice. As of March 9, 2007, approximately 160,000 shares at an average price of $26.48 per share have been repurchased under this program. Future repurchases will be reported in our quarterly and annual reports under Item 5 on a monthly basis.

We believe that cash generated from operations and borrowings under our credit agreement will be sufficient to fund our working capital and other cash flow requirements for at least the next 18 months. Our credit agreement expires on September 30, 2007.

Off-Balance Sheet Arrangements

We do not have any arrangements classified as off-balance sheet arrangements.

Contractual Obligations and Commercial Commitments

Our contractual obligations and commercial commitments include future minimum obligations under operating leases and purchase obligations. Our purchase obligations primarily consist of purchase orders for merchandise inventory, construction commitments related to our new distribution center and obligations associated with building out our stores. The future minimum payments for these obligations as of December 30, 2006 for periods subsequent to this date are as follows:

	Payments Due by Fiscal Period as of December 30, 2006						
	Total	**2007**	**2008**	**2009**	**2010**	**2011**	**Beyond**
				(In thousands)			
Operating lease obligations	347,886	42,222	44,106	43,432	42,016	38,590	137,520
Purchase obligations	44,719	44,421	228	60	5	4	
Total	$392,605	$86,644	$44,334	$43,492	$42,021	$38,594	$137,520

Inflation

We do not believe that inflation has had a material adverse impact on our business or operating results during the periods presented. We cannot assure you, however, that our business will not be affected by inflation in the future.

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Critical Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles requires the appropriate application of certain accounting policies, many of which require us to make estimates and assumptions about future events and their impact on amounts reported in our financial statements and related notes. Since future events and their impact cannot be determined with certainty, the actual results will inevitably differ from our estimates. Such differences could be material to the financial statements.

We believe application of accounting policies, and the estimates inherently required therein, are reasonable. These accounting policies and estimates are periodically reevaluated, and adjustments are made when facts and circumstances dictate a change. Historically, we have found our application of accounting policies to be appropriate, and actual results have not differed materially from those determined using necessary estimates.

Our accounting policies are more fully described in note 2 to our consolidated financial statements, which appear elsewhere in this annual report on Form 10-K. We have identified certain critical accounting policies which are described below.

Inventory

Inventory is stated at the lower of cost or market, with cost determined on an average cost basis. Historically, we have not conducted sales whereby we offer significant discounts or markdowns, nor have we experienced significant occurrences of obsolete or slow moving inventory. However, future changes in circumstances, such as changes in guest merchandise preference, could cause reclassification of inventory as obsolete or slow-moving inventory. The effect of this reclassification would be the recording of a reduction in the value of inventory to realizable values.

Throughout the year we record an estimated cost of shortage based on past historical results. Periodic physical inventories are taken and any difference between the actual physical count of merchandise and the recorded amount in our records are adjusted and recorded as shortage. Historically, the timing of the physical inventory has been near the end of the fiscal year so that no material amount of shortage was required to be estimated on activity between the date of the physical count and year-end. However, future physical counts of merchandise may not be at times at or near the end of a fiscal quarter or fiscal year-end, and our estimate of shortage for the intervening period may be material based on the amount of time between the date of the physical inventory and the date of the fiscal quarter or year-end.

Long-Lived Assets

If facts and circumstances indicate that a long-lived asset, including property and equipment, may be impaired, the carrying value is reviewed. If this review indicates that the carrying value of the asset will not be recovered as determined based on projected undiscounted cash flows related to the asset over its remaining life, the carrying value of the asset is reduced to its estimated fair value. No long-lived assets were impaired in fiscal 2006, 2005, or 2004. In fiscal 2004, we determined that one store which had been designated for closure would remain open. This determination resulted in the reversal of $0.1 million in impairment charges taken in fiscal 2001 for costs to be incurred upon the closing of the store. Impairment losses in the future are dependent on a number of factors such as site selection and general economic trends, and thus could be significantly different than historical results. To the extent our estimates for net sales, gross profit and store expenses are not realized, future assessments of recoverability could result in additional impairment charges.

Goodwill and Other Intangibles

The Company has adopted SFAS No. 142. Under the provisions of this standard, intangible assets deemed to have indefinite lives and goodwill are not subject to amortization. All other intangible assets are amortized over their estimated useful lives. Goodwill and other intangible assets not subject to amortization are tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. This testing requires comparison of carrying values to fair values, and when appropriate, the carrying value of impaired assets is reduced to fair value. We reviewed our goodwill and other intangible assets as of December 30, 2006 and determined that no impairment existed.

Revenue Recognition

Revenues from retail sales, net of discounts and excluding sales tax, are recognized at the time of sale. Guest returns have not been significant. Revenues from gift certificates are recognized at the time of redemption. Unredeemed gift cards are included in current liabilities on the consolidated balance sheets.

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We have an automated frequent shopper program in the United States, the Stuff Fur Stuff® club, whereby guests enroll in the program and receive one point for every dollar or partial dollar spent and after reaching 100 points receive a $10 discount on a future purchase. This program was automated in July 2006 and replaced our former Buy Stuff Program, which was a manual punch card system with limited tracking capability. The reward earned under the new program did not change. An estimate of the obligation related to the program, based on historical redemption rates, is recorded as deferred revenue and a reduction of net retail sales at the time of purchase. The deferred revenue obligation is reduced, and a corresponding amount is recognized in net retail sales, in the amount of and at the time of redemption of the $10 discount.

Under the previous Buy Stuff Program, the first card had no expiration date. Beginning in June 2002, and continuing each summer up to July 1, 2006, a series of cards was issued that had an expiration date of December 31 of the year following the year in which that series of cards was first issued. Beginning in July 2006, the automated Stuff Fur Stuff® club was introduced which provides greater visibility to the rewards earned by our guests and the historical redemption rates. We track redemptions of these various cards and use actual redemption rates by card series and historical results to estimate how much revenue to defer. We review these redemption rates and assess the adequacy of the deferred revenue account at the end of each fiscal quarter. Due to the estimates involved in these assessments, adjustments to the deferral rate are generally made no more often than bi-annually in order to allow time for more definite trends to emerge.

Based upon an assessment at the end of fiscal 2003, the deferred revenue account was adjusted downward by $1.1 million with a corresponding increase to net retail sales, an increase in net income of $0.7 million. Additionally, the amount of revenue being deferred beginning in fiscal 2004 was decreased by 0.2%, and by another 0.5% beginning with the third quarter of 2004, to give effect to the change in redemption experience. The changes made to the deferral rate in fiscal 2004 were prospective in nature with no impact on previously reported results of operations. Beginning with the second quarter of fiscal 2005, the amount of revenue being deferred was reduced by 0.1% on a prospective basis from its then current level due to further changes in the Company s redemption experience.

Based on the most recent assessment at the end of fiscal 2006, the deferred revenue account was adjusted downward by $3.6 million, effective at the beginning of fiscal 2006, with a corresponding increase to net sales, and a $2.2 million increase in net income. Additionally, the amount of revenue being deferred for future periods has been decreased by 0.6%, to give effect to the change in redemption experience and the increased visibility of the redemptions with the automated system. An additional 0.1% adjustment of the ultimate redemption rate at the end of fiscal 2006 for the current cards expiring on December 30, 2006 and December 29, 2007 would have an approximate impact of $0.5 million on the deferred revenue balance and net retail sales.

Recent Accounting Pronouncements

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 (FIN 48). FIN 48 establishes threshold and measurement attributes for financial statement measurement and recognition of tax positions taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We will adopt FIN 48 on December 31, 2006. We do not expect the adoption of FIN 48 will have a significant impact on the financial results of the Company and will not result in a significant cumulative effect adjustment to the December 31, 2006 balance of retained earnings.

In September 2006, the FASB issued SFAS 157, Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on assumptions that market participants would use in pricing the asset or liability. We are required to adopt SFAS 157 in the first quarter of 2008. We are currently assessing the financial impact of SFAS 157 on our consolidated financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our market risks relate primarily to changes in interest rates, and we bear this risk in two specific ways. First, our revolving credit facility carries a variable interest rate that is tied to market indices and, therefore, our results of operations and our cash flows can be impacted by changes in interest rates. Outstanding balances under our credit facility bear interest at our option of prime minus 1.0% or LIBOR plus 1.5%. We had no borrowings outstanding during fiscal 2006. Accordingly, a 100 basis point change in interest rates would result in no material change to our annual interest expense. The second component of interest rate risk involves the short term investment of excess cash in short term, investment grade interest-bearing securities. These investments are considered to be cash equivalents and are shown that way on our balance sheet. If there are changes in interest rates, those changes would affect the investment income we earn on these investments and, therefore, impact our cash flows and results of operations.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements and schedules are listed under Item 15(a) and filed as part of this annual report on Form 10-K.

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

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Bear and Chief Financial Bear, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this report. Our management, with the participation of our Chief Executive Bear and Chief Financial Bear also conducted an evaluation of our internal control over financial reporting to determine whether any changes occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Based on this evaluation, our management, including the Chief Executive Bear and Chief Financial Bear, concluded that our disclosure controls and procedures were effective as of December 30, 2006, the end of the period covered by this annual report.

It should be noted that our management, including the Chief Executive Bear and the Chief Financial Bear, do not expect that our disclosure controls and procedures or internal controls will prevent all error and all fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Management s Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with accounting principles generally accepted in the United States of America. With the participation of our Chief Executive Bear and our Chief Financial Bear, management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that our internal control over financial reporting was effective as of December 30, 2006.

In conduction our evaluation of the effectiveness of our internal control over financial reporting, we have excluded the acquisition of The Bear Factory Limited and Amsbra Limited (collectively, the U.K. Acquisition). Total revenues of these entities for the period from the respective acquisitions through December 30, 2006 were $32.8 million. These entities were acquired for total consideration of $39.4 million, subject to certain contingent purchase price adjustments. Refer to Note 3 to our consolidated financial statements for further discussion of the U.K. acquisition and the impact on our consolidated financial results.

The Company s independent registered public accounting firm has audited and issued their report on management s assessment of the Company s internal control over financial reporting. That report appears in this Item 9A.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Build-A-Bear Workshop, Inc.:

We have audited management s assessment, included in the accompanying Management s Report on Internal Control over Financial Reporting that Build-A-Bear Workshop, Inc. and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 30, 2006, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the Company s internal control over financial

reporting based on our audit.
We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.
A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.
Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.
In our opinion, management s assessment that the Company maintained effective internal control over financial reporting as of December 30, 2006, is fairly stated, in all material respects, based on criteria established in Internal Control Integrated Framework issued by COSO. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 30, 2006, based on criteria established in Internal Control Integrated Framework issued by COSO.
The Company acquired The Bear Factory Limited and Amsbra Limited, during the fiscal year ended December 30, 2006. Management excluded from its assessment of the effectiveness of the Company s internal control over financial reporting as of December 30, 2006, these entities internal control over financial reporting associated with total revenues of $32.8 million, included in the consolidated financial statements of the Company for the periods from the respective acquisitions through December 30, 2006. These entities were acquired for total consideration of $39.4 million, subject to certain contingent purchase price adjustments. Our audit of internal control over financial reporting of the Company also excluded an evaluation of the internal control over financial reporting of these entities.
We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of December 30, 2006, and December 31, 2005, and the related consolidated statements of operations, stockholders equity, and cash flows for each of the years in the three-year period ended December 30, 2006, and our report dated March 15, 2007 expressed an unqualified opinion on those consolidated financial statements.
/s/ KPMG LLP
St. Louis, Missouri
March 15, 2007

Changes in Internal Controls

There were no changes in internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) that occurred during the fourth quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

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PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Information concerning directors, appearing under the caption Board of Directors in our Proxy Statement (the Proxy Statement) to be filed with the SEC in connection with our Annual Meeting of Shareholders scheduled to be held on May 10, 2007 is incorporated by reference in response to this Item 10.

The information appearing under the caption Section 16(a) Beneficial Ownership reporting Compliance in the Proxy Statement is incorporated by reference in response to this Item 10.

Business Conduct Policy

The Board of Directors has adopted a Business Conduct Policy applicable to our directors, officers and employees, including all executive officers. The Business Conduct Policy has been posted in the Investor Relations section of our corporate web site at http://ir.buildabear.com. We intend to satisfy the amendment and waiver disclosure requirements under applicable securities regulations by posting any amendments of, or waivers to, the Business Conduct Policy on our web site.

The information appearing under the caption Code of Ethics in the Proxy Statement is incorporated by reference in response to this Item 10.

Executive Officers and Key Employees

Set forth below is the name, age, position and a brief account of the business experience of each of our executive officers and key employees as of March 9, 2007.

Name	Age	Position(s)
Maxine Clark	58	Chief Executive Bear and Chairman of the Board
Scott Seay	44	President and Chief Operating Officer Bear
Tina Klocke	47	Chief Financial Bear, Treasurer and Secretary
Teresa Kroll	52	Chief Marketing Bear
Paul Bundonis	45	Chief Workshop Bear

Maxine Clark has been our Chief Executive Bear since our inception in 1997, our President from our inception in 1997 to April 2004 and has served as Chairman of our board of directors since our conversion to a corporation in April 2000. From November 1992 until January 1996, Ms. Clark was the President of Payless ShoeSource, Inc. Prior to joining Payless, Ms. Clark spent over 19 years in various divisions of The May Department Stores Company in areas including merchandise development, merchandise planning, merchandise research, marketing and product development. Ms. Clark is a member of the Board of Directors of The J.C. Penney Company, Inc. and Chairman of its Corporate Governance Committee. She also serves on the Board of Trustees of the International Council of Shopping Centers and Washington University in St. Louis and on the Board of Directors of Barnes Jewish Hospital. Ms. Clark is Chairman of the Board of Directors of Teach for America St. Louis. She is also a member of the Committee of 200, an organization for women entrepreneurs around the world.

Scott Seay joined Build-A-Bear Workshop in May 2002 as Chief Workshop Bear and was named President and Chief Operating Bear in January 2007. Prior to joining us, Mr. Seay was Chief of Field Operations for Kinko s Inc., a national chain of copy centers, from April 1999 to May 2002. From April 1991 to April 1999, Mr. Seay held several operational roles including Senior Vice President of Operations West for CompUSA Inc., a computer retailer. From April 1983 to April 1991, Mr. Seay held several operational positions for The Home Depot, Inc.

Tina Klocke has been our Chief Financial Bear since November 1997, our Treasurer since April 2000, and Secretary since February 2004. Prior to joining us, she was the Controller for Clayton Corporation, a manufacturing company, where she supervised all accounting and finance functions as well as human resources. Prior to joining Clayton in 1990, she was the controller for Love Real Estate Company, a diversified investment management and development firm. She began her career in 1982 with Ernst & Young LLP.

Teresa Kroll has been our Chief Marketing Bear since September 2001. Prior to joining us Ms. Kroll was Vice President-Advertising for The WIZ, a unit of Cablevision, from 1999 to 2001. From 1995 to 1999, Ms. Kroll was Director of Marketing for Montgomery Ward Holding Corp., a department store retailer. From 1980 to 1994 Ms. Kroll held various administrative and marketing positions for Venture Stores, Inc.

Paul Bundonis joined Build-A-Bear Workshop in May 2006 as Managing Director, Western Region and was named Chief Workshop Bear in January 2007. Prior to joining us, Mr. Bundonis was President and Chief Operating Officer at Olly Shoes, a children s shoe retailer, from 2003 to 2006. From 2000 to 2003, Mr. Bundonis was Director Store Operations Planning and Development at Express (Limited Brands), a specialty retailer. From 1998 to 2000, he was Vice President Merchandise Planning and Replenishment at Zany Brainy, Inc., a specialty retailer. From 1979 to 1998, Mr. Bundonis held various operations positions at Eddie Bauer, Inc. and R.H. Macy, Inc.

Barry Erdos served as our President and Chief Operating Officer Bear during the 2006 fiscal year and until January 5, 2007. On January 5, 2007, Mr. Erdos resigned as President and Chief Operating Officer Bear. Also effective on January 5, 2007, Scott Seay was appointed President and Chief Operating Bear and Paul Bundonis assumed the role of Chief Workshop Bear.

ITEM 11. EXECUTIVE COMPENSATION

The information contained in the sections titled Executive Compensation and Information About the Board of Directors Board of Directors Compensation in the Proxy Statement is incorporated herein by reference in response to this Item 11.

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

The information contained in the section titled Security Ownership of Certain Beneficial Owners and Management in the Proxy Statement is incorporated herein by reference in response to this Item 12.

Equity Compensation Plan Information

Plan category	**(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights**	**(b) Weighted-average exercise price of outstanding options, warrants and rights**	**(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (1)**
Equity compensation plans approved by security holders	529,200	$ 16.10	2,530,420
Equity compensation plans not approved by security holders			
Total	529,200	$ 16.10	2,530,420

(1) The number of securities remaining available for future issuance under equity compensation plans includes 880,689 shares available for

issuance under our Associate Stock Purchase Plan (ASPP). Shares sold under our ASPP can be obtained from treasury stock, authorized but unissued shares or open market purchases of our common stock.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information contained in the section titled Certain Relationships and Related Party Transactions in the Proxy Statement is incorporated herein by reference in response to this Item 13.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information contained in the section titled Principal Accountant Fees and Policy Regarding Pre-Approval of Services Provided by the Independent Auditor in the Proxy Statement is incorporated herein by reference in response to Item 14.

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PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) *Financial Statements*

The financial statements and schedules set forth below are filed on the indicated pages as part of this annual report on Form 10-K.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Build-A-Bear Workshop, Inc.:

We have audited the accompanying consolidated balance sheets of Build-A-Bear Workshop, Inc. and subsidiaries (the Company) as of December 30, 2006 and December 31, 2005, and the related consolidated statements of operations, stockholders equity, and cash flows for each of the years in the three-year period ended December 30, 2006. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 30, 2006 and December 31, 2005, and the results of their operations and their cash flows for each of the years in the three-year period ended December 30, 2006, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 2 to the Consolidated Financial Statements, the Company adopted Statement of Financial Accounting Standards No. 123R Shared Based Payment , effective January 1, 2006.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 30, 2006, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 15, 2007 expressed an unqualified opinion on management s assessment of, and the effective operation of, internal control over financial reporting.

/s/ KPMG LLP
St. Louis, Missouri
March 15, 2007

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BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except share and per share data)

	December 30, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 53,109	$ 90,950
Inventories	50,905	40,157
Receivables	7,389	6,629
Prepaid expenses and other current assets	11,805	6,839
Deferred tax assets	2,388	3,232
Total current assets	125,596	147,807
Property and equipment, net	130,347	89,973
Note receivable from franchisee		4,518
Goodwill	36,927	
Other intangible assets, net	2,873	1,454
Other assets, net	4,027	2,356
Total Assets	$ 299,770	$ 246,108
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 46,761	$ 34,996
Accrued expenses	16,301	15,792
Gift cards and customer deposits	28,128	22,865
Deferred revenue	6,454	7,508
Total current liabilities	97,644	81,161
Deferred franchise revenue	2,297	2,306
Deferred rent	34,754	30,687
Other liabilities	352	586
Deferred tax liabilities	459	1,011
Commitments and contingencies See Note 12		
Stockholders equity:		
Preferred stock, par value $0.01. Shares authorized: 15,000,000; No shares issued or outstanding		
Common stock, par value $0.01. Shares authorized: 50,000,000; Issued and outstanding: 20,537,421 and 20,120,655 shares, respectively	205	201
Additional paid-in capital	88,866	85,259
Other comprehensive income	(997)	
Retained earnings	76,190	46,700
Notes receivable from officers		(151)
Unearned compensation		(1,652)

Total stockholders equity		164,264		130,357
Total Liabilities and Stockholders Equity	$	299,770	$	246,108

See accompanying notes to consolidated financial statements.

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BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in thousands, except share and per share data)

	Fiscal Year		
	2006	**2005**	**2004**
Revenues:			
Net retail sales	$ 432,572	$ 358,901	$ 300,469
Franchise fees	3,521	1,976	846
Licensing revenue	979	932	347
Total revenues	437,072	361,809	301,662
Costs and expenses:			
Cost of merchandise sold	227,509	180,373	150,903
Selling, general, and administrative	158,712	133,921	115,939
Store preopening	3,958	4,812	2,186
Interest expense (income), net	(1,530)	(1,710)	(299)
Total costs and expenses	388,649	317,396	268,729
Income before income taxes	48,423	44,413	32,933
Income tax expense	18,933	17,099	12,934
Net income	29,490	27,314	19,999
Cumulative dividends and accretion of redeemable preferred stock			1,262
Cumulative dividends of nonredeemable preferred stock			263
Net income available to common and participating preferred stockholders	$ 29,490	$ 27,314	$ 18,474
Net income allocated to common stockholders	$ 29,490	$ 27,314	$ 8,519
Net income allocated to participating preferred stockholders	$	$	$ 9,955
Earnings per common share:			
Basic	$ 1.46	$ 1.38	$ 2.30
Diluted	$ 1.44	$ 1.35	$ 1.07
Shares used in computing common per share amounts:			
Basic	20,169,814	19,735,067	3,702,365
Diluted	20,468,256	20,229,978	18,816,435

See accompanying notes to consolidated financial statements.

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BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY
(Dollars in thousands)

	Nonredeemable preferred stock Class A	Nonredeemable preferred stock Class B	Nonredeemable preferred stock Class C	Common stock	Additional paid-in capital	Other comprehensive income	Retained earnings	Notes receivable from officers	Unearned compensation	Total
Balance, January 3, 2004	24	20	50	5	10,918		10,649	(1,821)		19,845
Interest on notes receivable from officers					93			(93)		
Collection of notes receivable from officers								144		144
Cumulative dividends and accretion of redeemable preferred stock							(1,262)			(1,262)
Payment of cash dividend							(10,000)			(10,000)
Exercise of stock options and exchange of outstanding shares, net of tax benefit			(1)	4	460					463
Shares withheld in lieu of tax withholdings				(1)	(539)					(540)
Stock-based compensation related to stock options and restricted stock					1,984				(10)	1,974
Initial public offering, net of offering expenses				15	25,720					25,735
Conversion of redeemable and non-redeemable preferred stock to common stock	(24)	(20)	(49)	173	39,072					39,152
Net income							19,999			19,999
				196	77,708		19,386	(1,770)	(10)	95,510

Balance, January 1, 2005										
Interest on notes receivable from officers					26			(26)		
Collection of notes receivable from officers								1,645		1,645
Issuance of restricted common stock				1	2,436				(2,437)	
Employee stock purchases				1	1,670					1,671
Exercise of stock options, net of tax benefit				4	5,829					5,833
Shares withheld in lieu of tax withholdings				(1)	(2,410)					(2,411)
Stock-based compensation related to restricted stock									795	795
Net income							27,314			27,314
Balance, December 31, 2005	$	$	$	$ 201	$ 85,259	$	$ 46,700	$ (151)	$ (1,652)	$ 130,357
Reclassification of unearned compensation upon adoption of SFAS 123R					(1,652)				1,652	
Interest on notes receivable from officers					4			(4)		
Collection of notes receivable from officers								155		155
Issuance of restricted common stock				2	(2)					
Employee stock purchases				1	478					479
Exercise of stock options, net of tax benefit				2	2,780					2,782
Shares withheld in lieu of tax withholdings				(1)	(140)					(141)
					2,139					2,139

Stock-based compensation related to restricted stock										
Other comprehensive income						(997)				(997)
Net income							29,490			29,490
Balance, December 30, 2006	$	$	$	$ 205	$ 88,866	$ (997)	$ 76,190	$	$	$ 164,264

See accompanying notes to consolidated financial statements.

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BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)

	Fiscal Year 2006	2005	2004
Cash flows from operating activities:			
Net income	$ 29,490	$ 27,314	$ 19,999
Adjustments to reconcile net income to net cash from operating activities:			
Depreciation and amortization	22,394	17,592	14,948
Deferred taxes	(1,130)	(2,035)	(1,875)
Tax benefit from stock option exercises	(1,269)	3,091	410
Loss on disposal of property and equipment	82	526	533
Impairment of goodwill			97
Impairment charge (credit)			(54)
Stock-based compensation	2,139	795	1,974
Change in assets and liabilities:			
Inventories	(8,368)	(9,366)	(8,218)
Receivables	(1,826)	(2,804)	(1,629)
Prepaid expenses and other assets	(1,021)	(1,612)	(1,105)
Accounts payable	3,419	9,229	3,998
Accrued expenses and other liabilities	9,125	11,912	19,449
Net cash provided by operating activities	53,035	54,642	48,527
Cash flows from investing activities:			
Purchases of property and equipment	(52,577)	(31,083)	(16,494)
Purchases of other assets and other intangible assets	(2,063)	(1,569)	(1,238)
Loan to franchisee		(4,425)	
Purchase of business, net of cash acquired	(39,132)		
Net cash used in investing activities	(93,772)	(37,077)	(17,732)
Cash flows from financing activities:			
Exercise of employee stock options and employee stock purchases	2,112	4,413	52
Collection of notes receivable from officers	155	1,645	144
Payment of cash dividend			(10,000)
Tax benefit from stock option exercises	1,270		
Proceeds from initial public offering, net of offering costs			25,735
Net cash provided by financing activities	3,537	6,058	15,931
Effect of exchange rates on cash	(641)		
Net (decrease) increase in cash and cash equivalents	(37,841)	23,623	46,726
Cash and cash equivalents, beginning of year	90,950	67,327	20,601
Cash and cash equivalents, end of year	$ 53,109	$ 90,950	$ 67,327

Supplemental disclosure of cash flow information:			
Cash paid during the year for:			
Interest	$ 11	$ 79	$ 15
Income taxes	$ 18,969	$ 11,562	$ 13,578
Noncash transaction:			
Cumulative dividends and accretion of redeemable preferred stock	$	$	$ 1,262

See accompanying notes to consolidated financial statements.

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(1) Description of Business

Build-A-Bear Workshop, Inc. (the Company) is a specialty retailer of plush animals and related products. At December 30, 2006, the Company operated 271 stores (unaudited) located in the United States, Canada, the United Kingdom, and Ireland. The Company was formed in September 1997 and began operations in October 1997. The Company changed to a Delaware C Corporation on April 3, 2000. The Company previously operated as a Missouri Limited Liability Company.

During 2001, the Company and a third party formed Build-A-Bear Entertainment, LLC (BABE) for the purpose of promoting the Build-A-Bear Workshop brand and characters of the Company through certain entertainment media. Prior to February 2003, the Company owned 51% and was the managing member. BABE had no active operations for the period from December 29, 2001 through February 10, 2003. On February 10, 2003, the Company purchased, for $200,000, the 49% minority interest in BABE, which then became a wholly-owned subsidiary.

During 2002, the Company formed Build-A-Bear Workshop Franchise Holdings, Inc. (Holdings) for the purpose of entering into franchise agreements with companies in foreign countries other than Canada. Holdings is a wholly-owned subsidiary of the Company. Since 2002, Holdings has signed franchise agreements with third parties to open Build-A-Bear Workshop stores in various countries throughout the world. For each of the franchise agreements, Holdings received a one-time, nonrefundable fee that has been deferred and is being amortized over the life of the respective franchise agreement. Holdings also receives a percentage of all sales by the franchisees. As of December 30, 2006, the number of Build-A-Bear Workshop franchise stores that are open and operating in these countries is as follows (unaudited):

Japan	7
Australia	6
Denmark	5
Taiwan	3
Other	13

On April 2, 2006, Holdings acquired all of the outstanding shares of The Bear Factory Limited, a stuffed animal retailer in the United Kingdom, and Amsbra Limited, our former U.K. franchisee. During 2006, the Company formed Build-A-Bear Workshop UK Holdings, Ltd (UK Holdings) as the parent company to The Bear Factory and Amsbra. UK Holdings is a wholly-owned subsidiary of Holdings. The results of the acquisition s operations have been included in the consolidated financial statements since the date of acquisition. In conjunction with those transactions, we obtained 40 (unaudited) retail locations in the United Kingdom and Ireland. Amsbra operated 11 (unaudited) franchised Build-A-Bear Workshop stores located in the United Kingdom. Upon completion of the acquisition, all of the franchised locations in the United Kingdom became company-owned stores. Also during 2006, the Company formed Build-A-Bear Workshop Ireland and Build-A-Bear Workshop France as wholly-owned subsidiaries of Holdings.

During 2003, the Company formed Build-A-Bear Retail Management, Inc. (BABRM) for the purpose of providing purchasing, legal, information technology, accounting, and other general management services for Build-A-Bear Workshop stores. BABRM is a wholly-owned subsidiary of the Company.

(2) Summary of Significant Accounting Policies

A summary of the Company s significant accounting policies applied in the preparation of the accompanying consolidated financial statements follows:

(a) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Build-A-Bear Workshop, Inc. and its wholly-owned subsidiaries: Holdings, BAB Canada, BABE, and BABRM. All significant intercompany accounts are eliminated in consolidation.

(b) Fiscal Year

The Company operates on a 52- or 53-week fiscal year ending on the Saturday closest to December 31. The periods presented in these financial statements are the fiscal years ended December 30, 2006 (fiscal 2006), December 31, 2005 (fiscal 2005), and January

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1, 2005 (fiscal 2004). All fiscal years presented included 52 weeks. References to years in these financial statements relate to fiscal years or year ends rather than calendar years.

(c) Cash and Cash Equivalents

Cash and cash equivalents include cash and short-term highly liquid investments with an original maturity of three months or less.

The majority of the Company s cash and cash equivalents exceed federal deposit insurance limits. The Company has not experienced any losses in such accounts and management believes that the Company is not exposed to any significant credit risk on cash and cash equivalents.

(d) Inventories

Inventories are stated at the lower of cost or market, with cost determined on an average-cost basis.

(e) Receivables

Receivables consist primarily of amounts due to the Company in relation to tenant allowances, corporate product sales, franchisee royalties and product sales, and licensing revenue. The Company assesses the collectibility of all receivables on an ongoing basis by considering its historical credit loss experience, current economic conditions, and other relevant factors. Based on this analysis, the Company has determined that no material allowance for doubtful accounts was necessary at either December 30, 2006 or December 31, 2005.

(f) Property and Equipment

Property and equipment consist of leasehold improvements, furniture and fixtures, and computer equipment and software and are stated at cost. Leasehold improvements are depreciated using the straight-line method over the shorter of the useful life of the assets or the life of the lease which is generally ten years. Furniture and fixtures and computer equipment are depreciated using the straight-line method over the estimated service lives ranging from three to seven years. Computer software is amortized using the straight-line method over a period of three years. New store construction deposits are recorded at the time the deposit is made as construction-in-progress and reclassified to the appropriate property and equipment category at the time of completion of construction, when operations of the store commence. Maintenance and repairs are expensed as incurred and improvements are capitalized. Gains or losses on the disposition of fixed assets are recorded upon disposal.

(g) Note Receivable from Franchisee

The 2005 note receivable from franchisee consists of principal and accrued interest related to a loan made to one of the Company s international franchisees. The note is stated at face value plus accrued interest. The note receivable was included in the purchase price of the U.K. acquisition on April 2, 2006.

(h) Goodwill

The Company has adopted SFAS No. 142. Under the provisions of this standard, goodwill is not subject to amortization. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. This testing requires comparison of carrying values to fair values, and when appropriate, the carrying value of impaired assets is reduced to fair value. We reviewed our goodwill as of December 30, 2006 and determined that no impairment existed.

(i) Other Intangible Assets

Other intangible assets consist primarily of costs related to trademarks and other intellectual property. Trademarks and other intellectual property represent third-party costs that are capitalized and amortized over their estimated lives ranging from one to ten years using the straight-line method.

(j) Other Assets

Other assets consist primarily of deferred leasing fees and deferred costs related to franchise agreements. Deferred leasing fees are initial, direct costs related to the Company s operating leases and are amortized over the term of the related leases. Amortization expense related to other assets was $0.5 million, $0.3 million, and $0.3 million for 2006, 2005, and 2004, respectively.

(k) Long-lived Assets

Whenever facts and circumstances indicate that the carrying value of a long-lived asset may not be recoverable, the carrying value is reviewed. If this review indicates that the carrying value of the asset will not be recovered, as determined based on projected undiscounted cash flows related to the asset over its remaining life, the carrying value of the asset is reduced to its estimated fair value.

(l) Deferred Rent

Certain of the Company s operating leases contain predetermined fixed escalations of minimum rentals during the original lease terms. For these leases, the Company recognizes the related rental expense on a straight-line basis over the life of the lease and records the difference between the amounts charged to operations and amounts paid as deferred rent. The Company also receives certain lease incentives in conjunction with entering into operating leases. These lease incentives are recorded as deferred rent at the beginning of the lease term and recognized as a reduction of rent expense over the lease term. In addition, certain of the Company s leases contain future contingent increases in rentals. Such increases in rental expense are recorded in the period that it is probable that store sales will meet or exceed the specified target that triggers contingent rental expense.

(m) Franchises

The Company defers initial, one-time nonrefundable franchise fees and amortizes them over the life of the respective franchise agreements, which extend for periods up to 10 years. Continuing franchise fees are recognized as revenue as the fees are earned. The Company defers direct and incremental costs incurred with third parties when entering into franchise agreements and amortizes them over the life of the respective franchise agreements.

(n) Retail Revenue Recognition

Net retail sales are net of discounts, exclude sales tax, and are recognized at the time of sale. Shipping and handling costs billed to customers are included in net retail sales.

Revenues from the sale of gift cards are recognized at the time of redemption. Unredeemed gift cards are included in gift cards and customer deposits on the consolidated balance sheets. The company escheats a portion of unredeemed gift cards according to Delaware escheatment regulations that require remittance of the cost of merchandise portion of unredeemed gift cards over five years old. The difference between the value of gift cards and the amount escheated is recorded as a reduction in selling, general, and administrative expenses in the consolidated statement of operations.

The Company has an automated frequent shopper program in the United States, the Stuff Fur Stuff® club, whereby guests enroll in the program and receive one point for every dollar or partial dollar spent and after reaching 100 points receive a $10 discount on a future purchase. This program was automated in July 2006 and replaced the former Buy Stuff Program, which was a manual punch card system with limited tracking capability. The reward earned under the new program did not change. An estimate of the obligation related to the program, based on historical redemption rates, is recorded as deferred revenue and a reduction of net retail sales at the time of purchase. The deferred revenue obligation is reduced, and a corresponding amount is recognized in net retail sales, in the amount of and at the time of redemption of the $10 discount.

Under the previous Buy Stuff Program, the first card had no expiration date. Beginning in June 2002, and continuing each summer up to July 1, 2006, a series of cards was issued that had an expiration date of December 31 of the year following the year in which that series of cards was first issued. Beginning in July 2006, the automated Stuff Fur Stuff® club was introduced which provides greater visibility to the rewards earned by our guests and the historical redemption rates. Management tracks redemptions of these various cards and uses actual redemption rates by card series and historical results to estimate how much revenue to defer. Management reviews these redemption rates and assesses the adequacy of the deferred revenue account at the end of each fiscal quarter. Due to the estimates involved in these assessments, adjustments to the deferral rate are generally made no more often than bi-annually in order to allow time for more definite trends to emerge.

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Based upon an assessment at the end of fiscal 2003, the deferred revenue account was adjusted downward by $1.1 million with a corresponding increase to net retail sales, an increase in net income of $0.7 million. Additionally, the amount of revenue being deferred beginning in fiscal 2004 was decreased by 0.2%, and by another 0.5% beginning with the third quarter of 2004, to give effect to the change in redemption experience. The changes made to the deferral rate in fiscal 2004 were prospective in nature with no impact on previously reported results of operations. Beginning with the second quarter of fiscal 2005, the amount of revenue being deferred was reduced by 0.1% on a prospective basis from its then current level due to further changes in the Company s redemption experience.

Based on the most recent assessment at the end of fiscal 2006, the deferred revenue account was adjusted downward by $3.6 million, effective at the beginning of fiscal 2006, with a corresponding increase to net sales, and a $2.2 million increase in net income. Additionally, the amount of revenue being deferred for future periods has been decreased by 0.6%, to give effect to the change in redemption experience and the increased visibility of the redemptions with the automated system. An additional 0.1% adjustment of the ultimate redemption rate at the end of fiscal 2006 for the current cards expiring on December 30, 2006 and December 29, 2007 would have an approximate impact of $0.5 million on the deferred revenue balance and net retail sales.

(o) Cost of Merchandise Sold

Cost of merchandise sold includes the cost of the merchandise, royalties paid to licensors of third party branded merchandise, store occupancy cost, including store depreciation, freight costs from the manufacturer to the store, cost of warehousing and distribution, packaging, damages and shortages, and shipping and handling costs incurred in shipment to customers.

(p) Selling, General, and Administrative Expenses

Selling, general, and administrative expenses include store payroll and related benefits, advertising, credit card fees, and store supplies, as well as central office management payroll and related benefits, travel, information systems, accounting, insurance, legal, and public relations. It also includes depreciation and amortization of central office leasehold improvements, furniture, fixtures, and equipment, as well as amortization of trademarks and intellectual property.

(q) Store Preopening Expenses

Store preopening expenses, including store set-up, certain labor and hiring costs, and rental charges incurred prior to store openings are expensed as incurred.

(r) Advertising

Production costs of commercials and programming are charged to operations in the period during which the production is first aired. The costs of other advertising, promotion and marketing programs are charged to operations in the period the program takes place. Advertising expense was $31.0 million, $27.2 million, and $22.7 million for fiscal years 2006, 2005 and 2004, respectively.

(s) Income Taxes

Income taxes are accounted for using a balance sheet approach known as the asset and liability method. The asset and liability method accounts for deferred income taxes by applying the statutory tax rates in effect at the date of the consolidated balance sheets to differences between the book basis and the tax basis of assets and liabilities.

(t) Earnings Per Share

Certain classes of preferred stock were entitled to participate in cash dividends on common stock prior to their conversion. For purposes of calculating basic earnings per share, undistributed earnings were allocated to common and participating preferred shares on a pro rata basis. Basic earnings per share is determined by dividing net income allocated to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects the potential dilution that could occur if options to issue common stock or conversion rights of preferred stocks were exercised. In periods in which the inclusion of such instruments is anti-dilutive, the effect of such securities is not given consideration.

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All outstanding classes of preferred stock were converted to common stock in conjunction with the completion of the Company s initial public offering on October 28, 2004.

(u) Stock-Based Compensation

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R). SFAS 123R requires companies to recognize the cost of awards of equity instruments, such as stock options and restricted stock, based on the fair value of those awards at the date of grant and eliminates the choice to account for employee stock options under Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25). The Company adopted SFAS 123R effective January 1, 2006 using the modified prospective method and, as such, results for prior periods have not been restated. Under this method, in addition to reflecting compensation expense for new share-based awards, expense is also recognized to reflect the remaining service period of awards that had been included in pro forma disclosures in prior periods. Prior to January 1, 2006, the fair value of restricted stock awards was expensed by the Company over the vesting period, while compensation expense for stock options was recognized over the vesting period only to the extent that the grant date market price of the stock exceeded the exercise price of the options.

For 2006, selling, general and administrative expense includes $2.1 million ($1.4 million after tax) of stock-based compensation expense which had a $0.07 impact on both basic and diluted earnings per share. Of this amount, $0.2 million ($0.2 after tax) is attributable to the Company s adoption of SFAS 123R. This incremental expense from the adoption of SFAS 123R did not reduce basic or diluted earnings per share based upon the insignificance of the expense. The additional stock-based compensation expense not related to the adoption of SFAS 123R was related to the vesting of restricted stock awards.

As of December 30, 2006, there was $4.4 million of total unrecognized compensation expense related to nonvested restricted stock awards and options which is expected to be recognized over a weighted-average period of 2.75 years.

The following table illustrates the effect on net income and earnings per share as if the Company had applied the fair value method of SFAS No. 123, *Accounting for Stock-Based Compensation* (SFAS 123), prior to January 1, 2006 (in thousands except per share amounts):

	2005	2004
Net income:		
As reported	$ 27,314	$ 19,999
Add stock-based employee compensation expense recorded, net of related tax effects	489	1,446
Deduct stock-based employee compensation expense under fair value-based method, net of related tax effects	(2,758)	(2,643)
Pro Forma	$ 25,045	$ 18,802
Basic earnings per common share:		
As reported	$ 1.38	$ 2.30
Pro forma	$ 1.27	$ 2.03
Diluted earnings per common share:		
As reported	$ 1.35	$ 1.07
Pro forma	$ 1.24	$ 1.02

The fair value of each option was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions: (a) dividend yield of 0%; (b) expected volatility of 50%; (c) risk-free interest rate of 3.5%; and (d) a weighted average expected life of 6.3 years for 2005 and 9.4 years for 2004. The weighted average grant date fair value of options granted during fiscal 2005 and fiscal 2004 was $17.23 and $8.63, respectively. There were no new options granted in fiscal 2006. The pro forma disclosures above utilize the accelerated expense attribution method under FASB Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans An Interpretation of APB Opinions No. 15 and 25*. Upon adoption of SFAS 123R, the Company made a policy decision that the straight-line expense attribution method would be utilized for all future stock-based compensation awards with graded vesting.

On October 21, 2005, the Compensation Committee of the Board of Directors of the Company approved accelerated vesting of all unvested stock options which were granted prior to March 9, 2005. These options have exercise prices ranting from $20.00 to $34.65 per share. Options to purchase 174,056 shares of the Company s stock became exercisable on October 21, 2005 as a result of this acceleration, including 71,000 shares held by the Company s named executive officers. Of these options, 173,056 had exercise prices in excess of the current market value at the time of the acceleration of vesting.

The Compensation Committee s decision to accelerate the vesting of the accelerated options was based upon the issuance of SFAS 123R. The acceleration of the vesting of these stock options enabled the Company to avoid compensation charges related to these options in subsequent periods of the effective date under the provisions of SFAS 123R.

The aggregate compensation expense that would have been recorded subsequent to the adoption of SFAS 123R, but is eliminated as a result of the acceleration of the vesting of these options, is approximately $1.8 million ($1.1 million net of tax). This amount is instead reflected in the above pro forma disclosures for 2005.

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Prior to the adoption of SFAS 123R, the Company presented the benefit of all tax deductions resulting from the exercise of stock options and restricted stock awards as operating cash flows in the consolidated statements of cash flows. SFAS 123R requires the benefits of tax deductions in excess of grant-date fair value be reported as a financing cash flow, rather than as an operating cash flow. Excess tax benefits of $1.3 million, which were classified as a financing cash inflow in fiscal 2006, would have been classified as an operating cash inflow if the Company had not adopted SFAS 123R.

(v) Fair Value of Financial Instruments

For purposes of financial reporting, management has determined that the fair value of financial instruments, including cash and cash equivalents, receivables, accounts payable, and accrued expenses, approximates book value at December 30, 2006 and December 31, 2005.

(w) Use of Estimates

The preparation of the consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of property and equipment and intangibles, inventories, the valuation of assets and liabilities in the purchase price allocation for business combinations and deferred income tax assets and the determination of deferred revenue under the Company s frequent shopper program.

(x) Sales Tax Policy

The Company s revenues in the consolidated statement of operations are net of sales taxes.

(y) Foreign Currency Translation

Assets and liabilities of the Company s foreign operations are translated at the exchange rate in effect at the balance sheet date, while revenues and expenses are translated at average rates prevailing during the years. Translation adjustments are reported in other comprehensive income, a separate component of stockholders equity.

(z) Recent Accounting Pronouncements

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 (FIN 48). FIN 48 establishes threshold and measurement attributes for financial statement measurement and recognition of tax positions taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company will adopt FIN 48 on December 31, 2006. Management does not expect the adoption of FIN 48 will have a significant impact on the financial results of the Company and will not result in a significant cumulative effect adjustment to the December 31, 2006 balance of retained earnings.

In September 2006, the FASB issued SFAS 157, Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on assumptions that market participants would use in pricing the asset or liability. The Company is required to adopt SFAS 157 in the first quarter of 2008. The Company is currently assessing the financial impact of SFAS 157 on its consolidated financial statements.

(3) Business Acquisition

On April 2, 2006, the Company acquired all of the outstanding shares of The Bear Factory Limited (Bear Factory), a stuffed animal retailer in the United Kingdom, and Amsbra Limited (Amsbra), the Company s former U.K. franchisee (collectively, the U.K. Acquisition). The results of the U.K. Acquisition operations have been included in the consolidated financial statements since that date. In conjunction with those transactions, we obtained 40 (unaudited) retail locations in the United Kingdom and Ireland. The aggregate cash purchase price for the U.K. Acquisition was $39.4 million, excluding cash acquired of $0.3 million. In addition to the cash purchase price, the

Company had previously advanced $4.5 million to Amsbra as a note receivable. The amount of this note receivable and the related accrued interest is a non-cash component of the purchase price.

The Company has not completed its assessment of the U.K. Acquisition assets and liabilities. Until that assessment is complete, the allocation of the purchase price is preliminary and may be subject to revisions.

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The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition (in thousands):

Current assets	$ 6,497
Property and equipment	6,192
Goodwill	31,727
Intangibles	1,824
Total assets acquired	46,240
Current liabilites assumed	(8,607)
Loan previously advanced	4,517
Total purchase price	$ 42,150

The following unaudited pro forma summary presents the Company s revenue, net income, basic earnings per share and diluted earnings per share as if the U.K. Acquisition had occurred on January 2, 2005 (in thousands, except per share data):

	Fiscal 2006	Fiscal 2005
Revenue	$ 446,140	$ 404,057
Net Income	27,735	21,189
Basic earnings per common share:	$ 1.38	$ 1.07
Diluted earnings per common share:	$ 1.36	$ 1.05

Pro forma adjustments have been made to reflect depreciation and amortization using estimated asset values recognized after applying purchase accounting adjustments.

This pro forma information is presented for informational purposes only and is not necessarily indicative of actual results had the acquisition been effected at the beginning of the respective periods presented, and is not necessarily indicative of future results.

(4) Comprehensive Income

Comprehensive income for fiscal 2006 and fiscal 2005 was $30.1 million and $27.3 million, respectively. The difference between comprehensive income and net income resulted from foreign currency translation adjustments.

(5) Property and Equipment

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

	2006	2005
Land	$ 2,261	$
Furniture and fixtures	33,938	19,727
Computer hardware	15,649	12,655
Building	14,970	
Leasehold improvements	122,043	98,991
Computer software	12,988	7,250
Construction in progress	2,200	5,853
	204,049	144,476
Less accumulated depreciation	73,702	54,503

	$ 130,347	$ 89,973

For 2006, 2005, and 2004, depreciation expense was $20.5 million, $16.4 million, and $13.8 million, respectively.

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(6) Goodwill

On April 2, 2006, the Company acquired all of the outstanding shares of The Bear Factory Limited (Bear Factory), a stuffed animal retailer in the United Kingdom, and Amsbra Limited (Amsbra), the Company s former U.K. franchisee (collectively, the U.K. Acquisition). The purchase was recorded in accordance with SFAS No. 141, Business Combinations and is reported as a component of the Company s retail segment. The following table summarizes the Company s goodwill (in thousands):

U.K. Acquisition	$ 31,727
Acquisition costs	1,005
Severance costs	785
	33,517
Effect of foreign currency translation	3,410
Goodwill, as of December 30, 2006	$ 36,927

There was no tax-deductible goodwill as of December 30, 2006.

(7) Other Intangible Assets

Other intangible assets consist of the following (in thousands):

	2006	2005
Trademarks and other intellectual property at cost	$ 8,897	$ 6,026
Less accumulated amortization	6,024	4,572
Total, net	$ 2,873	$ 1,454

Trademarks and intellectual property are amortized over three to ten years. Amortization expense related to trademarks and intellectual property was $1.4 million in 2006 and $0.9 million each year for 2005 and 2004. Estimated amortization expense related to other intangible assets as of December 30, 2006, for each of the years in the subsequent five year period and thereafter is: 2007- $1.3 million; 2008 $0.8 million; 2009 $0.4 million; 2010 $0.1 million; 2011 $0.1 million and all remaining years $0.2 million.

Trademarks and intellectual property acquired in the U.K. Acquisition were $2.0 million at cost and had $0.5 million in amortization in fiscal 2006.

(8) Accrued Expenses

Accrued expenses consist of the following (in thousands):

	2006	2005
Accrued wages, bonuses and related expenses	$ 3,559	$ 3,926
Sales tax payable	5,384	4,217
Current income taxes payable	6,482	6,653
Accrued rent and related expenses	876	996
	$ 16,301	$ 15,792

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(9) Income Taxes

The components of the provision for income taxes are as follows (in thousands):

	2006	2005	2004
Current:			
Federal	$ 15,660	$ 15,770	$ 12,432
State	2,156	2,584	2,035
Foreign	2,220	780	342
Deferred:			
Federal	(1,282)	(1,757)	(1,617)
State	(119)	(278)	(258)
Foreign	298		
Income tax expense	$ 18,933	$ 17,099	$ 12,934

The income tax expense is different from the amount computed by applying the U.S. statutory Federal income tax rates to income before income taxes. The reasons for these differences are as follows (in thousands):

	2006	2005	2004
Net income before taxes	$ 48,421	$ 44,413	$ 32,933
UK net operating loss no tax benefit	1,452		
Income before income taxes	49,873	44,413	32,933
U.S. statutory Federal income tax rate	35%	35%	35%
Computed income taxes	17,456	15,545	11,527
State income taxes, net of Federal tax benefit	1,325	1,498	1,155
Other	152	56	252
Income tax expense	$ 18,933	$ 17,099	$ 12,934
Effective tax rate	39.1%	38.5%	39.3%

Temporary differences that gave rise to deferred income tax assets and liabilities are as follows (in thousands):

	2006	2005
Deferred income tax assets:		
Deferred revenue	$ 3,529	$ 4,240
Accrued rents	3,409	3,210
Deferred compensation	829	380
Intangible assets	1,283	1,173
Stock compensation	234	350
Accrued severance	207	
Net operating loss carryovers	435	
Other	223	211
	10,149	9,564
Less: valuation allowance	(435)	
Total deferred income tax assets	9,714	9,564

Deferred income tax liabilities:		
Depreciation	(6,001)	(6,963)
Other	(389)	(380)
Total deferred income tax liabilities	(6,390)	(7,343)
Net deferred income tax asset	$ 3,324	$ 2,221

As of December 30, 2006, the Company has recognized a net operating loss for its wholly-owned U. K. subsidiaries of $1.5 million. The tax impact of that loss is $0.4 million based on a local tax rate in the U. K. of 30%. The entire benefit of that loss has been reduced by a valuation allowance. At the time when the loss is utilized, that valuation allowance will be relieved. There are no statutory expiration limits on net operating loss carryforwards in the U.K. The Company had no valuation allowance at December 31, 2005.

(10) Long-Term Debt

On June 30, 2006, the Company amended its previous line of credit with a bank increasing their borrowing capacity from $15 million to $30 million. The amended line of credit has an effective date of June 30, 2006 with a maturity date of September 30, 2007. Borrowings under the amended line of credit (the credit agreement) are not collateralized, but availability under the credit agreement can be limited by the lender based on the Company s levels of accounts receivable, inventory, and property and equipment. The credit agreement requires the Company to comply with certain financial covenants, including maintaining a minimum tangible net worth, maintaining a minimum fixed charge coverage ratio (as defined in the credit agreement) and not exceeding a maximum funded debt to earnings before interest, depreciation and amortization ratio. The credit agreement also places certain restrictions on indebtedness, liens, guarantees, redemptions, mergers, acquisitions or sale of assets, loans, transactions with affiliates, and investments. It also prohibits the Company from declaring dividends without the bank s prior consent, unless such payment of dividends would not violate any terms of the loan agreement. Borrowings bear interest at the Company s option of prime minus 1.0% or LIBOR plus 1.5%.

There was no outstanding balance under the credit agreement at December 30, 2006 or December 31, 2005 other than a standby letter of credit for $1.1 million. Giving effect to this standby letter of credit, there was $28.9 million available for borrowing under the credit agreement at December 30, 2006 and December 31, 2005.

(11) Commitments and Contingencies

(a) Operating Leases

The Company leases its retail stores, web fulfillment site, and corporate offices under agreements which expire at various dates through 2023. The majority of leases contain provisions for base rent plus contingent payments based on defined sales. Total office and retail store base rent expense was $40.5 million, $23.8 million, and $19.9 million, and contingent rents were $1.5 million, $1.8 million, and $1.2 million for 2006, 2005, and 2004, respectively.

Future minimum lease payments at December 30, 2006, were as follows (in thousands):

2007	$ 42,222
2008	44,106
2009	43,432
2010	42,016
2011	38,590
Subsequent to 2011	137,520
	$ 347,886

(b) Litigation

In the normal course of business, the Company is subject to certain claims or lawsuits. Management is not aware of any claims or lawsuits that will have a material adverse effect on the consolidated financial position or results of operations of the Company.

(12) Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except share and per share date):

	2006	2005	2004
Net income	$ 29,490	$ 27,314	$ 19,999
Cumulative dividends and accretion of redeemable preferred stock			1,262
Cumulative dividends of nonredeemable preferred stock			263
Net income available to common and participating preferred stockholders	29,490	27,314	18,474
Dividends and accretion related to dilutive preferred stock:			
Series A-1			113
Series A-2			20
Series A-3			101
Series A-4			29
Series A-5			293
Series B-4			41
Series D			928
Total dividends and accretion			1,525
	$ 29,490	$ 27,314	$ 19,999
Net income allocated to common stockholders	$ 29,490	$ 27,314	$ 8,519
Net income allocated to participating preferred stockholders	$	$	$ 9,955
Weighted average number of common shares outstanding	20,169,814	19,735,067	3,702,365
Weighted average number of participating preferred shares outstanding			7,805,238
Weighted average number of common shares outstanding	20,169,814	19,735,067	3,702,365
Effect of dilutive securities:			
Stock options	236,316	420,280	556,545
Restricted stock	62,125	74,631	205,845
	20,468,256	20,229,978	4,464,755
Convertible preferred shares:			
Series A-1			1,203,221
Series A-2			148,017
Series A-3			1,016,444
Series A-4			217,641
Series A-5			1,122,950
Series B-1			226,182
Series B-2			1,193,595
Series B-3			255,467
Series B-4			1,318,130

Series C						4,084,723
Series D						3,365,310
Total dilutive convertible preferred shares						14,151,680
Weighted average number of common shares dilutive		20,468,256		20,229,978		18,616,435
Earnings per share:						
Basic:						
Per common share	$	1.46	$	1.38	$	2.30
Per participating preferred share	$		$		$	1.28
Diluted	$	1.44	$	1.35	$	1.07

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In calculating diluted earnings per share for fiscal 2006, options to purchase 166,588 shares of common stock were outstanding at the end of the period, but were not included in the computation of diluted earnings per share due to their anti-dilutive effect.

In calculating diluted earnings per share for fiscal 2005, options to purchase 173,560 shares of common stock were outstanding at the end of the period, but were not included in the computation of diluted earnings per share due to their anti-dilutive effect. An additional 51,750 shares of restricted common stock were outstanding at the end of the period, but excluded from the calculation of diluted earnings per share due to their anti-dilutive effect under provisions of Statement of Financial Accounting Standards No. 128, *Earnings per Share*.

No options were excluded from the diluted earnings per share calculation for fiscal 2004.

(13) Stock Incentive Plans

On April 3, 2000, the Company adopted the 2000 Stock Option Plan (the Plan). In 2003, the Company adopted the Build-A-Bear Workshop, Inc. 2002 Stock Incentive Plan, and, in 2004, the Company adopted the Build-A-Bear Workshop, Inc. 2004 Stock Incentive Plan (collectively, the Plans).

Under the Plans, as amended, up to 3,700,000 shares of common stock were reserved and may be granted to employees and nonemployees of the Company. The Plan allows for the grant of incentive stock options, nonqualified stock options, and restricted stock. Options granted under the Plan expire no later than 10 years from the date of the grant. The exercise price of each incentive stock option shall not be less than 100% of the fair value of the stock subject to the option on the date the option is granted. The exercise price of the nonqualified options shall be determined from time to time by the compensation committee of the board of directors (the Committee). The vesting provision of individual options is at the discretion of the Committee and generally ranges from one to four years.

(a) Stock Options

The following table is a summary of the balance and activity for the Plans related to stock options for the periods presented:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding, January 3, 2004	1,067,549	$ 4.82		
Granted:				
Exercise price less than fair market value	302,234	8.78		
Exercise price equal to fair market value	2,000	20.00		
Exercised	268,912	2.05		
Forfeited	63,463	8.05		
Outstanding, January 1, 2005	1,039,408	6.52		
Granted:				
Exercise price less than fair market value	218,292	32.73		
Exercised	475,970	5.76		
Forfeited	13,107	28.87		
Outstanding, December 31, 2005	768,623	14.06		
Exercised	208,951	7.23		
Forfeited	30,472	25.46		
Outstanding, December 30, 2006	529,200	$ 16.10	6.0	$ 6,310

Options Exercisable As Of:					
December 30, 2006	525,450	16.05	5.9	$	6,291

The total intrinsic value of options exercised in fiscal 2006 and fiscal 2005 was approximately $4.3 million and $10.5 million, respectively. The Company generally issues new shares to satisfy option exercises.

The Company granted options during 2004 at an exercise price of $8.78 per share, which had been determined to be the fair value of its common stock at the time based on an independent appraisal. Subsequent to such grants, the Company determined that the fair value of the underlying common stock should have been deemed to be approximately $15.00 per share. As a result of this

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determination, this option issuance generated stock-based compensation of $1.9 million to be recognized over the vesting period of the 302,234 underlying options. These options became fully vested upon completion of the Company s initial public offering on October 28, 2004. Accordingly, all unrecognized compensation expense related to this grant was recognized at that time and is reflected in the consolidated statement of operations for the fiscal year ended January 1, 2005.

In May of 2004, a former officer of the Company surrendered 48,964 shares of Class C preferred stock in exchange for the exercise of 255,600 stock options with exercise prices ranging from $0.47 to $6.10 per share. In conjunction with this transaction, the vesting of 9,400 options with an exercise price of $6.04 per share was accelerated by one calendar month. Stock compensation costs of $26,000 are reflected in the consolidated statements of operations for the modification of the terms of these options. The Company also extended the due date of a loan made to the same former officer. The loan was originally due upon the earlier of the officer s separation date from the Company or September 19, 2006. The officer separated from the Company during 2004. On the date of separation, the due date of the loan was extended until September 19, 2006. The loan was collected in full on November 24, 2004.

In May of 2004, the Company accelerated the vesting of 5,625 options with an exercise price of $9.10 per share. The options were held by a former member of the Company s board of directors. The options were originally scheduled to vest at a rate of 1,875 per year on April 24 of each year through April 24, 2007. Simultaneously with this acceleration, the Company allowed the former director to exercise 7,500 options with an exercise price of $9.10 per share for no consideration. The 7,500 options consisted of the 5,625 accelerated options plus 1,875 previously vested options. At the time of this modification, the fair value of the Company s common stock was $8.78 per share. Accordingly, the Company recognized $66,000 in compensation expense at the time of this modification, which is reflected in the consolidated statements of operations.

Shares available for future option, non-vested stock and restricted stock grants were 1,649,731 and 1,796,166 at the end of 2006 and 2005, respectively.

(b) Restricted Stock

The following table is a summary of the balance and activity for the Plans related to unvested restricted stock granted as compensation to employees and directors for the periods presented:

	Number of Shares	Weighted Average Grant Date Fair Value per Award
Outstanding, January 1, 2005 and January 3, 2004		$
Granted	82,946	32.37
Outstanding, December 31, 2005	82,946	32.37
Granted	230,702	29.18
Vested	42,705	30.60
Forfeited	43,490	29.27
Outstanding, December 30, 2006	227,453	$ 30.06

On April 3, 2000, the Company issued 274,815 shares of restricted common stock to an officer of the Company in exchange for a promissory note of $1,236,667 that bore interest at 6.60% per annum. Both principal and interest were collected in full in April 2005.

On September 19, 2001, the Company issued 40,982 shares of contractually restricted common stock to two officers of the Company in exchange for nonrecourse promissory notes totaling $249,990 that bear interest at 4.82% per annum. Both principal and interest are due September 2006. On November 24, 2004, the Company collected all outstanding principal and interest related to 20,491 shares of this restricted stock. On September 19, 2006, the

Company collected all outstanding principal and interest on the remaining 20,291 shares of this restricted stock. The collection of these funds removed all remaining restrictions from those shares.

On November 17, 2004, the Company granted 330 shares of non-vested common stock to a member of its board of directors as compensation for services. The shares were issued subject to a restriction of continued service on the board of directors, and all restrictions lapsed one year from the grant date. The fair value of the non-vested stock at the date of grant was $30.33 per share.

In March 2005, the Company granted 51,750 shares of restricted, non-vested stock to certain executives of the Company. The shares vest ratably over a four year period from the date of grant if a certain net income level is achieved by the Company in fiscal 2005 and the executives remain employed by the Company over the vesting period. The executives are entitled to vote these restricted shares and will be eligible for participation in any dividends declared during the vesting period. The net income level required for vesting was achieved in fiscal 2005. Under the provisions of APB Opinion No. 25 and related interpretations, the compensation related to these shares was adjusted to the market value ($29.64 per share) of the Company s common stock as of December 31, 2005, the date the performance condition was satisfied. During 2005, 1,000 shares of the non-vested stock were forfeited by an executive due to the cessation of the executive s employment with the Company. In July 2005, 1,000 shares of non-vested stock were issued under the same terms as the March 2005 grant noted above to a new executive who joined the Company. At December 31, 2005, the total fair value of these restricted stock grants was approximately $1.5 million. During fiscal 2005, the Company recorded compensation expense of approximately $0.6 million related to these restricted stock grants. The 51,750 shares of non-vested stock were excluded from the calculation of diluted earnings per share because the achievement of the specified net income level was not known until the end of fiscal 2005. These non-vested shares will be included in the calculation of diluted earnings per share beginning January 1, 2006.

During 2005, an additional 31,196 shares of non-vested stock were granted to various members of the Company s board of directors as compensation for services. The shares were issued subject to a restriction of continued service on the board of directors, and all restrictions lapse over a period from one to three years from the grant date. The weighted average grant date fair value of these non-vested shares was $28.95 per share.

During 2006, 195,040 of non-vested restricted stock were granted to employees of the Company. The shares vest over a period of 4 years from the grant date at a grant date fair value of $29.14. An additional 28,321 shares of non-vested stock were granted to various members of the Company s board of directors as compensation for services. The shares were issued subject to a restriction of continued service on the board of directors and all restrictions lapse over a period of one to three year from the grant date. In September 2006, a one time discretionary grant of 4,941 shares of restricted stock were granted to an executive of the Company for continued valued contributions to the Company and vest over a period of one year from the grant date. In May 2006, 2,400 shares of restricted stock were granted to a newly hired employee. The shares vest over a period of 4 years from the grant date.

The aggregate unearned compensation expense related to restricted stock was $4.3 million as of December 30, 2006. Based on the vesting provisions of the underlying equity instruments, future compensation expense related to previously issued restricted stock at December 30, 2006 was as follows (in thousands):

2007	$ 1,887
2008	1,190
2009	1,035
2010	237
	$ 4,349

The outstanding restricted and non-vested stock is included in the number of outstanding shares on the face of the consolidated balance sheets, but is treated as outstanding stock options for accounting purposes. The shares of restricted and non-vested stock, accounted for as options, are included in the calculation of diluted earnings per share using the treasury stock method, with the proceeds equal to the sum of unrecognized compensation cost and amounts to be collected from the outstanding loans related to the restricted stock, where applicable.

(c) Associate Stock Purchase Plan

In October 2004, the Company adopted an Associate Stock Purchase Plan (ASPP). Under the ASPP, substantially all full-time employees are given the right to purchase shares of the Company s common stock, subject to certain limitations, at 85% of the lesser of the fair market value on the purchase date or the beginning of each purchase period. Up to 1,000,000 shares of the Company s common stock are available for issuance under the ASPP. The employees of the Company purchased 34,488 shares at $20.00 per share through the ASPP during fiscal 2006. The expense recorded related to the ASPP during fiscal 2006 was determined using the Black-Scholes option pricing model and the provision of FASB Technical Bulletin 97-1, *Accounting under Statement 123 for Certain Employee Stock Purchase Plans with a Look-Back Option* (FTB 97-1), as amended by SFAS 123R. The assumptions used in the option pricing model for fiscal 2006 were: (a) dividend yield of 0%; (b) volatility of 20%; (c) risk-free interest rate of 6.0%; and (d) an expected life of 0.25 years. Prior to the adoption of SFAS 123R, the ASPP was considered noncompensatory and no expense was recorded in the consolidated statement of operations.

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(14) Stockholders Equity

(a) Reorganization and Preferred Stock Sales

Effective April 3, 2000, the Company reorganized from an LLC to a C Corporation. The existing LLC members received a total of 9,482,482 shares of Series A, B, and C convertible nonredeemable preferred stock and 217,519 shares of common stock in exchange for their member units.

On April 5, 2000, the Company issued a total of 2,666,666 shares of Series A and B convertible redeemable preferred stock in exchange for $9,837,876 in cash and $1,934,485 in a promissory note from a related party. The note was subsequently collected in full within 30 days of issuance. The proceeds are net of the costs associated with the preferred stock sales of $227,632.

From September through December 2001, the Company issued a total of 3,467,337 shares of Series D convertible redeemable preferred stock in exchange for $21,024,016 in cash. The cash proceeds are net of the costs associated with the preferred stock sales of $141,911.

(b) Preferred Stock

Prior to the Company s initial public offering, 25,000,000 shares of preferred stock were authorized. Preferred stock consisted of various series of Class A, B, C, and D preferred stock. Each class had various dividend, liquidation, and redemption rights as summarized below:

Series of Preferred Stock	Defined Liquidation Rights	Defined Cumulative Dividends	Shares Issued and Outstanding as of January 3, 2004	Liquidation Preference as of January 3, 2004 (in thousands)
A-1	$ 2.451890	0.171632	1,137,898	$ 3,522
A-2	3.556556	0.248959	139,981	629
A-3	2.600746	0.182052	961,263	3,156
A-4	3.484283	0.243900	205,824	905
A-5	5.649780	0.395485	1,061,986	7,575
B-1	1.808051	0.000000	275,352	498
B-2	1.720493	0.000000	1,453,072	2,500
B-3	2.305925	0.000000	311,003	717
B-4	3.739067	0.000000	1,604,680	6,000
C-1	0.105315	0.000000	3,418,306	360
C-2	0.973290	0.000000	1,385,507	1,349
C-3	0.720934	0.000000	194,276	140
D	6.100000	0.427000	3,467,337	24,471
			15,616,485	$ 51,822

During 2004, $1.3 million was recorded to increase the carrying value of the Series A-5, B-4, and D redeemable preferred stock to its redemption value. This includes cumulative dividends of $1.1 million and accretion of equity issuance costs of $0.2 million for 2004 for the redeemable preferred stock. Cumulative dividends in arrears for the nonredeemable preferred stock totaled approximately $1.7 million at January 3, 2004 and approximately $2.0 million at the date of conversion in conjunction with the initial public offering.

As of August 10, 2004, the Certificate of Incorporation was amended primarily with respect to the liquidation and redemption preferences of the Series A and Series D preferred stock as well as the dividend rights for all series of preferred stock. Previously, Series A and Series D preferred stock accrued a dividend and any accrued and unpaid dividends were added to the original liquidation preference and redemption amounts for these series. Additionally, these series had certain dividend preference rights over other classes of stock.

The amended Certificate of Incorporation effectively set the liquidation preferences and redemption amounts for the Series A and Series D stock to be equal to the original amounts plus the amounts of accrued and unpaid dividends as of July 31, 2004. Additionally, any dividend preferences or restrictions on all series of preferred stock were removed and all series of preferred stock participate on an as converted basis ratably with common stock for any declared dividends.

In August 2004, following the amendment of the Certificate of Incorporation, the Company paid a cash dividend of $10.0 million to the common and preferred stockholders. The dividend equated to $0.55 per share for all classes of stock.

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All shares of preferred stock, including shares of preferred stock issuable in exchange for accrued but unpaid dividends, were converted into 17,316,689 shares of common stock upon the completion of the Company s initial public offering.

(c) Initial Public Offering

On October 28, 2004, the Company completed an initial public offering (the offering) of 7,482,000 shares of common stock, of which 5,982,000 shares were sold by selling shareholders, at a price of $20.00 per share. The proceeds to the Company from the offering, after underwriting discounts and offering costs, were approximately $25.7 million. In conjunction with the offering, all shares of preferred stock, including shares of preferred stock issuable in exchange for accrued but unpaid dividends, were converted into 17,316,689 shares of common stock.

As a result of the initial public offering, the Company s charter was amended to authorize 50,000,000 shares of $0.01 par value common stock and 15,000,000 shares of $0.01 par value preferred stock.

(d) Share Activity

The following table summarizes the changes in outstanding shares of all series of common and preferred stock for fiscal 2004, 2005 and 2006:

	Redeemable Preferred Stock			Nonredeemable Preferred Stock			Common
	Class A	**Class B**	**Class D**	**Class A**	**Class B**	**Class C**	**Stock**
Shares as of December January 3, 2004	1,061,986	1,604,680	3,467,337	2,444,966	2,039,427	4,998,089	533,316
Exercise of stock options and exchange of outstanding shares						(48,964)	268,912
Shares withheld in lieu of tax withholdings							(61,463)
Issuance of restricted common stock							330
Conversion of preferred stock to common stock	(1,061,986)	(1,604,680)	(3,467,337)	(2,444,966)	(2,039,427)	(4,949,125)	17,316,689
Additional shares issued in the offering							1,500,000
Shares as of January 1, 2005							19,557,784
Employee stock purchases							84,823
Exercise of stock options							475,970
Shares withheld in lieu of tax							(80,868)

withholdings	
Issuance of restricted common stock	82,946
Shares as of December 31, 2005	20,120,655
Employee stock purchases	34,488
Exercise of stock options	208,621
Shares withheld in lieu of tax withholdings	(13,683)
Forfeiture of restricted common stock	(43,362)
Issuance of restricted common stock	230,702
Shares as of December 30, 2006	20,537,421

(15) Employee Benefit Plans

(a) 401(k) Savings Plan

During 2000, the Company established a defined contribution plan that conforms to IRS provisions for 401(k) plans. The Build-A-Bear Workshop, Inc. Employees Savings Trust covers associates who work 1,000 hours or more in a year and have attained age 21. The Company, at the discretion of its board of directors, can provide for a Company match on the first 6% of employee deferrals. For 2006, 2005, and 2004, the Company provided a match of 30% on the first 6% of employee deferrals totaling $0.3 million, $0.3 million, and $0.2 million, respectively. The Company match vests over a five-year period.

(16) Related-Party Transactions

The Company bought fixtures for new stores and furniture for the corporate offices from a related party. The total payments to this related party for fixtures and furniture amounted to $2.7 million, $3.3 million, and $1.9 million in 2006, 2005, and 2004, respectively. The Company leased part of its corporate office from the same related party in 2004. Rent under this lease amounted to $0.1 million 2004. As of December 30, 2005 nothing was due to this related party. The total due to this related party as of December 31, 2005 was $0.1 million.

The Company paid $0.8 million in 2004 for construction management services to an entity controlled by a stockholder holding in excess of 5% of one class of the Company s capital stock prior to the initial public offering. The Company leased one of its retail stores from this same related party in fiscal 2003. Subsequent to the initial public offering, this stockholder no longer owns in excess of 5% of any class of the Company s capital stock. As a result, the entity controlled by this stockholder is no longer considered a related party. The Company plans to continue to use the same entity for construction management services in the future.

The Company paid $0.4 million 2004 for design and other creative services to a stockholder holding in excess of 5% of one class of the Company s capital stock prior to the initial public offering. Subsequent to the initial public offering, this stockholder no longer owns in excess of 5% of any class of the Company s capital stock. As a result, the stockholder is no longer considered a related party. The Company plans to continue to use this stockholder for design and other creative services in the future.

The Company made charitable contributions of $1.0 million, $0.8 million and $0.2 million in 2006, 2005 and 2004, respectively, to charitable foundations controlled by the executive officers of the Company. The total due to the charitable foundations as of December 30, 2006 and December 31, 2005 was $0.2 million.

(17) Major Vendors

Three vendors accounted for approximately 83%, 86%, and 85% of inventory purchases in 2006, 2005, and 2004, respectively.

(18) Segment Information

The Company s operations are conducted through three reportable segments consisting of retail, international franchising, and licensing and entertainment. The retail segment includes the operating activities of company-owned stores in the United States, Canada, the United Kingdom and Ireland, and other retail delivery operations, including the Company s web store and non-traditional store locations such as baseball ballparks. The international franchising segment includes the licensing activities of the Company s franchise agreements with store locations in Europe, Asia, and Australia. The licensing and entertainment segment has been established to market the naming and branding rights of the Company s intellectual properties for third party use. These operating segments represent the basis on which the Company s chief operating decision-maker regularly evaluates the business in assessing performance, determining the allocation of resources and the pursuit of future growth opportunities. The operating segments have discrete sources of revenue, different capital structures and different cost structures. The reporting segments follow the same accounting policies used for the Company s consolidated financials statements.

Following is a summary of the financial information for the Company s reporting segments (in thousands):

	Retail	International Franchising	Licensing & Entertainment	Total
Fiscal 2004				
Net sales to external customers	$ 300,469	$ 846	$ 347	$ 301,662
Net income (loss) before income taxes	33,796	(990)	127	32,933
Capital expenditures	16,545	49		16,594
Depreciation and amortization	14,438	510		14,948
Fiscal 2005				
Net sales to external customers	358,901	1,976	932	361,809
Net income (loss) before income taxes	43,764	119	530	44,413
Capital expenditures	30,987	46	50	31,083
Depreciation and amortization	17,039	552	1	17,592
Fiscal 2006				
Net sales to external customers	432,571	3,521	979	437,071
Net income before income taxes	27,609	1,794	86	29,489
Capital expenditures	52,525	34	18	52,577
Depreciation and amortization	21,683	699	12	22,394
Total Assets as of:				
December 30, 2006	$ 295,337	$ 2,683	$ 1,750	$ 299,770
December 31, 2005	$ 235,754	$ 9,279	$ 1,075	$ 246,108

The Company s reportable segments are primarily determined by the types of products and services that they offer. Each reportable segment may operate in many geographic areas. The Company allocates revenues to geographic areas based on the location of the customer or franchisee. The following schedule is a summary of the Company s sales to external customers and long-lived assets by geographic area (in thousands):

	North America	United Kingdom & Ireland	Other	Total
Fiscal 2004				
Net sales to external customers	$ 300,781	$ 169	$ 712	$ 301,662
Property and equipment, net	75,815			75,815
Fiscal 2005				
Net sales to external customers	359,615	471	1,723	361,809
Property and equipment, net	89,924		49	89,973
Fiscal 2006				
Net sales to external customers	400,832	32,717	3,522	437,071
Property and equipment, net	$ 115,779	$ 14,549	$ 19	$ 130,347

(19) Subsequent Event

On February 20, 2007 the Company announced a $25 million share repurchase program of outstanding common stock over the next twelve months. The program was authorized by the Company s board of directors. Purchases may be made in the open market or in privately negotiated transactions, with the level and timing of activity depending on market conditions, other investment opportunities, and other factors. Purchases may be increased, decreased or discontinued at any time without notice.

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(a)(2) *Financial Statement Schedules*

No additional Financial Statement Schedules are filed as a part of this report pursuant to Item 8 and Item 15(d).

(a)(3) *Exhibits.*

The following is a list of exhibits filed as a part of the Annual Report on Form 10-K:

Exhibit Number	Description
2.1	Agreement and Plan of Merger dated April 3, 2000 between Build-A-Bear Workshop, L.L.C. and the Registrant (incorporated by reference from Exhibit 2.1 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
3.1	Third Amended and Restated Certificate of Incorporation (incorporated by reference from Exhibit 3.1 of our Current Report on Form 8-K, filed on November 11, 2004)
3.2	Amended and Restated Bylaws (incorporated by reference from Exhibit 3.4 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
4.1	Specimen Stock Certificate (incorporated by reference from Exhibit 4.1 to Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
4.2	Stock Purchase Agreement by and among the Registrant, Catterton Partners IV, L.P., Catterton Partners IV Offshore, L.P. and Catterton Partners IV Special Purpose, L.P. and the Purchasers named therein dated as of April 3, 2000 (incorporated by reference from Exhibit 4.2 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
4.3	Stock Purchase Agreement by and among the Registrant and the other Purchasers named therein dated as of September 21, 2001 (incorporated by reference from Exhibit 4.3 to our Registration Statement on Form S- 1, filed on August 12, 2004, Registration No. 333-118142)
4.4	Amended and Restated Registration Rights Agreement, dated September 21, 2001 by and among Registrant and certain stockholders named therein (incorporated by reference from Exhibit 4.5 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.1*	Build-A-Bear Workshop, Inc. 2000 Stock Option Plan (incorporated by reference from Exhibit 10.1 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.1.1*	Form of Incentive Stock Option Agreement under the Build-A-Bear Workshop, Inc. 2000 Stock Option Plan (incorporated by reference from Exhibit 10.1.1 to Pre-Effective Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
10.1.2*	Form of Nonqualified Stock Option Agreement under the Build-A-Bear Workshop, Inc. 2000 Stock Option Plan (incorporated by reference from Exhibit 10.1.2 to Pre-Effective Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
10.2*	Build-A-Bear Workshop, Inc. 2002 Stock Incentive Plan, as amended (incorporated by reference from Exhibit 10.2 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.2.1*	

	Form of Manager-Level Incentive Stock Option Agreement under the Build-A-Bear Workshop, Inc. 2002 Stock Option Plan (incorporated by reference from Exhibit 10.2.1 to Pre-Effective Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
10.2.2*	Form of Nonqualified Stock Option Agreement under the Build-A-Bear Workshop, Inc. 2002 Stock Option Plan (incorporated by reference from Exhibit 10.2.2 to Pre-Effective Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
10.3*	Build-A-Bear Workshop, Inc. 2004 Stock Incentive Plan (incorporated by reference from Exhibit 10.3 to Pre-Effective Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
10.3.1*	Form of Incentive Stock Option Agreement under the Build-A-Bear Workshop, Inc. 2004 Stock Incentive Plan (incorporated by reference from Exhibit 10.3.1 to Pre-Effective Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
10.3.2*	Form of Director Nonqualified Stock Option Agreement under the Build-A-Bear Workshop, Inc. 2004 Stock Incentive Plan (incorporated by reference from Exhibit 10.3.2 to Pre-Effective Amendment No. 3 to our Registration Statement on Form S-l, filed on October 1, 2004, Registration No. 333-118142)
10.3.3*	Model Incentive Stock Option Agreement Under the Registrant s 2004 Stock Incentive Plan (incorporated by reference from Exhibit 10.3.3 to Pre-Effective Amendment No. 5 to our Registration Statement on Form S-l, filed on October 12, 2004, Registration No. 333-118142)
10.3.4*	Form of Employee Nonqualified Stock Option Agreement under the Registrant s 2004 Stock Incentive Plan (incorporated by reference from Exhibit 10.3.4 to Pre-Effective Amendment No. 5 to our Registration Statement on Form S-l, filed on October 12, 2004, Registration No. 333-118142)
10.3.5*	Form of the Restricted Stock Agreement under the Registrant s 2004 Stock Incentive Plan (incorporated by

Exhibit Number	Description
	reference from Exhibit 10.3.5 to Pre-Effective Amendment No. 5 to our Registration Statement on Form S-1, filed on October 12, 2004, Registration No. 333-118142)
10.3.6*	Amended and Restated Build-A-Bear Workshop, Inc 2004 Stock Incentive Plan (incorporated by reference from Exhibit 10.1 on our Current Report on Form 8-K, filed on August 1, 2006)
10.4*	Employment, Confidentiality and Noncompete Agreement dated May 1, 2004 between Maxine Clark and the Registrant (incorporated by reference from Exhibit 10.4 to Pre-Effective Amendment No. 2 to our Registration Statement on Form S-l, filed on September 20, 2004, Registration No. 333-118142)
10.4.1*	First Amendment dated February 22, 2006 to the Employment, Confidentiality and Noncompete Agreement dated May 1, 2004 between Maxine Clark and the Registrant (incorporated by reference from Exhibit 10.4.1 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.5*	Employment, Confidentiality and Noncompete Agreement dated April 13, 2004 between Barry Erdos and the Registrant (incorporated by reference from Exhibit 10.5 to Pre-Effective Amendment No. 2 to our Registration Statement on Form S-l, filed on September 20, 2004, Registration No. 333-118142)
10.5.1*	First Amendment dated February 22, 2006 to the Employment, Confidentiality and Noncompete Agreement dated April 13, 2004 between Barry Erdos and the Registrant (incorporated by reference from Exhibit 10.5.1 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.5.2*	Separation Agreement and General Release dated January 5, 2007 between Barry Erdos and the Registrant (incorporated by reference from Exhibit 10.1 to our Current Report on Form 8-K, filed on January 5, 2007)
10.6*	Employment, Confidentiality and Noncompete Agreement dated March 7, 2004 between Tina Klocke and the Registrant (incorporated by reference from Exhibit 10.6 to Pre-Effective Amendment No. 2 to our Registration Statement on Form S-l, filed on September 20, 2004, Registration No. 333-118142)
10.6.1*	First Amendment dated February 22, 2006 to the Employment, Confidentiality and Noncompete Agreement dated March 7, 2004 between Tina Klocke and the Registrant (incorporated by reference from Exhibit 10.6.1 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.7*	Employment, Confidentiality and Noncompete Agreement dated July 9, 2001 between John Burtelow and the Registrant (incorporated by reference from Exhibit 10.7 to Pre-Effective Amendment No. 2 to our Registration Statement on Form S-l, filed on September 20, 2004, Registration No. 333-118142)
10.7.1*	First Amendment dated March 28, 2005 to Employment, Confidentiality and Noncompete Agreement dated July 9, 2001 between John Burtelow and the Registrant (incorporated by reference from Exhibit 10.1 to our Current Report on Form 8-K, filed on April 1, 2005)
10.8*	Employment, Confidentiality and Noncompete Agreement dated as of March 7, 2004 between Scott Seay and the Registrant (incorporated by reference from Exhibit 10.8 to Pre-Effective Amendment No. 2 to our Registration Statement on Form S-l, filed on September 20, 2004, Registration No. 333-118142)

10.8.1*	First Amendment dated February 22, 2006 to the Employment, Confidentiality and Noncompete Agreement dated March 7, 2004 between Scott Seay and the Registrant (incorporated by reference from Exhibit 10.8.1 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.8.2*	Second Amendment dated January 5, 2007 to the Employment, Confidentiality and Noncompete Agreement dated March 7, 2004 between Scott Seay and the Registrant (incorporated by reference from Exhibit 10.2 to our Current Report on Form 8-K, filed on January 5, 2007)
10.9*	Employment, Confidentiality and Noncompete Agreement dated September 10, 2001 between Teresa Kroll and the Registrant (incorporated by reference from Exhibit 10.9 to Pre-Effective Amendment No. 2 to our Registration Statement on Form S-l, filed on September 20, 2004, Registration No. 333-118142)
10.9.1*	First Amendment dated February 22, 2006 to the Employment, Confidentiality and Noncompete Agreement dated September 10, 2001 between Teresa Kroll and the Registrant (incorporated by reference from Exhibit 10.9.1 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.10*	Form of Indemnification Agreement between the Registrant and its directors and executive officers (incorporated by reference from Exhibit 10.11 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.11	Third Amendment to Loan Documents among the Registrant, Shirts Illustrated, LLC, Build-A-Bear Workshop Franchise Holdings, Inc., Build-A-Bear Entertainment, LLC, Build-A-Bear Retail Management, LLC (incorporated by reference from Exhibit 10.12 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.11.1	Fifth Amendment to Loan Documents among the Registrant, Shirts Illustrated, LLC, Build-A-Bear Workshop Franchise Holdings, Inc., Build-A-Bear Entertainment, LLC, Build-A-Bear Retail Management, LLC (incorporated by reference from Exhibit 10.1 of our Current Report on Form 8-K, filed on July 10, 2006)
10.12	Third Amended and Restated Loan Agreement between the Registrant, Shirts Illustrated, LLC, Build-A-Bear Workshop Franchise Holdings, Inc., Build-A-Bear Entertainment, LLC, and Build-A-Bear Retail Management, Inc., as borrowers, and U.S. Bank National Association, as Lender, entered into on September 27, 2005 with an effective date of May 31, 2005 (incorporated by reference from Exhibit 10.1 to our Current Report on Form 8-K, filed on October 3, 2005)

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Exhibit Number	Description
10.13	Second Amended and Restated Revolving Credit Note dated May 31, 2005 by the Registrant, Shirts Illustrated, LLC, Build-A-Bear Workshop Franchise Holdings, Inc., Build-A-Bear Entertainment, LLC, and Build-A-Bear Retail Management, Inc., as Borrowers, in favor of U.S. Bank National Association (incorporated by reference from Exhibit 10.2 to our Current Report on Form 8-K, filed on October 3, 2005)
10.13.1	Third Amended and Restated Revolving Credit Note dated June 30, 2006 by the Registrant, Build-A-Bear Workshop Franchise Holdings, Inc., Build-A-Bear Entertainment, LLC, Build-A-Bear Retail Management, Inc., and Build-A-Bear UK Holdings Ltd., as Borrowers, in favor of U.S. Bank National Association (incorporated by reference from Exhibit 10.2 to our Current Report on Form 8-K, filed on July 10, 2006)
10.14*	Restricted Stock Purchase Agreement dated April 3, 2000 by and between Maxine Clark and the Registrant (incorporated by reference from Exhibit 10.16 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.15*	Secured Promissory Note of Maxine Clark in favor of the Registrant, dated April 3, 2000 (incorporated by reference from Exhibit 10.17 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.16*	Repayment and Stock Pledge Agreement dated April 3, 2000 by and between Maxine Clark and the Registrant (incorporated by reference from Exhibit 10.18 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.17*	Restricted Stock Purchase Agreement dated September 19, 2001 by and between Tina Klocke and the Registrant (incorporated by reference from Exhibit 10.22 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.18*	Secured Promissory Note of Tina Klocke in favor of the Registrant, dated September 19, 2001 (incorporated by reference from Exhibit 10.23 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.19*	Repayment and Stock Pledge Agreement dated September 19, 2001 by and between Tina Klocke and the Registrant (incorporated by reference from Exhibit 10.24 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.20	Public Warehouse Agreement dated April 5, 2002 between the Registrant and JS Logistics, Inc., as amended (incorporated by reference from Exhibit 10.25 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.20.1	Second Amendment dated June 16, 2005 to the Public Warehouse Agreement dated April 5, 2002 between the Registrant and JS Warehousing, Inc. (incorporated by reference from Exhibit 10.2 to our Quarterly Report on Form 10-Q for the fiscal quarter ended on April 2, 2005)
10.20.2	Second Amendment dated June 16, 2005 to the Public Warehouse Agreement dated April 5, 2002 between the Registrant and JS Warehousing, Inc. (incorporated by reference from Exhibit 10.2 to our

	Quarterly Report on Form 10-Q for the fiscal quarter ended July 2, 2005)
10.21	Agreement for Logistics Services dated as of February 24, 2002 by and among the Registrant and HA Logistics, Inc. (incorporated by reference from Exhibit 10.26 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.21.1	Letter Agreement extending Agreement for Logistics Services between HA Logistics, Inc. and the Registrant dated March 22, 2005 (incorporated by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the fiscal quarter ended April 2. 2005)
10.21.2	Letter Agreement extending Agreement for Logistics Services between HA Logistics, Inc. and the Registrant dated May 3, 2005 (incorporated by reference from Exhibit 10.4 to our Quarterly Report on Form 10-Q for the fiscal quarter ended April 2, 2005)
10.21.3	Letter Agreement dated June 7, 2005 amending the Agreement for Logistics Services dated February 24, 2002 by and among the Registrant and HA Logistics, Inc. (incorporated by reference from Exhibit 10.1 to our Quarterly Report on Form 10-Q for the fiscal quarter ended July 2, 2005)
10.22	Lease Agreement dated as of June 21, 2001 between the Registrant and Walt Disney World Co. (incorporated by reference from Exhibit 2.1 of our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.23	Amendment and Restatement of Sublease dated as of June 14, 2000 by and between NewSpace, Inc. and the Registrant (incorporated by reference from Exhibit 10.28 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.24	Lease dated May 5, 1997 between Smart Stuff, Inc. and Hycel Partners I, L.P. (incorporated by reference from Exhibit 10.29 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.25	Agreement dated October 16, 2002 between the Registrant and Hycel Properties Co., as amended (incorporated by reference from Exhibit 10.30 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.26	Letter Agreement dated September 30, 2003 between the Registrant and Hycel Properties Co. (incorporated by reference from Exhibit 10.30.1 to Pre-Effective Amendment No. *5* to our Registration Statement on Form S-l, filed on October 12, 2004, Registration No. 333-118142)
10.27	Construction Management Agreement dated November 10, 2003 by and between the Registrant and Hycel

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Exhibit Number	Description
	Properties Co. (incorporated by reference from Exhibit 10.31 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.28	Agreement dated July 19, 2001 between the Registrant and Adrienne Weiss Company (incorporated by reference from Exhibit 10.32 to our Registration Statement on Form S-l, filed on August 12, 2004, Registration No. 333-118142)
10.29	Lease between 5th Midtown LLC and the Registrant dated July 21, 2004 (incorporated by reference from Exhibit 10.33 to Pre-Effective Amendment No. 1 to our Registration Statement on Form S-l, filed on September 10, 2004, Registration No. 333-118142)
10.30	Exclusive Patent License Agreement dated March 12, 2001 by and between Tonyco, Inc. and the Registrant (incorporated by reference from Exhibit 10.34 to Pre-Effective Amendment No. 2 to our Registration Statement on Form S-l, filed on September 20, 2004, Registration No. 333-118142)
10.31	Standard Form Industrial Building Lease dated August 28, 2004 between First Industrial, L.P. and the Registrant (incorporated by reference from Exhibit 10.35 to Pre-Effective Amendment No. 4 to our Registration Statement on Form S-l, filed on October 5, 2004, Registration No. 333-118142)
10.32	Loan Agreement by and between Amsbra, Ltd., as Borrower, and Build-A-Bear Workshop Franchise Holdings, Inc., as Lender, entered into on October 4, 2005 with an effective date of September 26, 2005 (incorporated by reference from Exhibit 10.1 to our Current Report on Form 8-K, filed on October 11, 2005)
10.33	Revolving Credit Note by Amsbra, Ltd., as Borrower, in favor of Build-A-Bear Workshop Franchise Holdings, Inc., dated as of September 26, 2005 (incorporated by reference from Exhibit 10.2 to our Current Report on Form 8-K, filed on October 11, 2005)
10.34	Debenture dated October 11, 2005 by and between Amsbra, Ltd. and Build-A-Bear Workshop Franchise Holdings, Inc. (incorporated by reference from Exhibit 10.3 to our Current Report on Form 8-K, filed on October 11, 2005)
10.35	Facility Construction Agreement dated December 22, 2005 between the Registrant and Duke Construction Limited Partnership (incorporated by reference from Exhibit 10.35 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.36	Real Estate Purchase Agreement dated December 19, 2005 between Duke Realty Ohio and the Registrant (incorporated by reference from Exhibit 10.36 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.37*	Description of Board Compensation for Non-Management Directors effective November 10, 2005 (incorporated by reference from Exhibit 10.1 from our Current Report on Form 8-K, filed on November 16, 2005)
10.38	Share Purchase Agreement dated March 3, 2006 between the Hamleys Group Limited, Build-A-Bear Workshop UK Holdings Limited and The Bear Factory Limited (incorporated by reference from Exhibit

	10.38 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.39	Sale and Purchase Agreement dated March 3, 2006 between the Registrant, Build-A-Bear Workshop UK Holdings Limited, the selling shareholders of Amsbra, Ltd. and Andrew Mackay (incorporated by reference from Exhibit 10.39 to our Annual Report on Form 10-K for the year ended December 31, 2005)
10.40*	Employment, Confidentiality and Noncompete Agreement dated January 16, 2007 between Paul Bundonis and the Registrant (incorporated by reference from Exhibit 10.1 to our Current Report on Form 8-K, filed on January 18, 2007)
10.41*	Rules of the Build-A-Bear Workshop, Inc. Share Option Scheme (incorporated by reference from Exhibit 10.1 to our Current Report on Form 8-K, filed on February 9, 2007)
10.42*	Nonqualified Deferred Compensation Plan
11.1	Statement regarding computation of earnings per share (incorporated by reference from Note 12 of the Registrant s audited consolidated financial statements included herein)
13.1	Annual Report to Shareholders for the Fiscal Year Ended December 30, 2006 (The Annual Report, except for those portions which are expressly incorporated by reference in the Form 10-K, is furnished for the information of the Commission and is not deemed filed as part of the Form 10-K)
21.1	List of Subsidiaries of the Registrant
23.1	Consent of KPMG LLP
31.1	Rule 13a-14(a)/15d-14(a) certification (pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, executed by the Chief Executive Bear)
31.2	Rule 13a-14(a)/15d-14(a) certification (pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, executed by the Chief Financial Bear)
32.1	Section 1350 Certification (pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, executed by the Chief Executive Bear)
32.2	Section 1350 Certification (pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, executed by the Chief Financial Bear)

* Management contract or compensatory plan or arrangement.

Confidential treatment requested as to certain portions filed separately with the Securities and

Exchange
Commission.

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BUILD-A-BEAR WORKSHOP, INC.
SIGNATURES

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

BUILD-A-BEAR WORKSHOP, INC.

(Registrant)

Date: March 15, 2007

By: /s/ Maxine Clark
Maxine Clark
Chief Executive Bear

By: /s/ Tina Klocke
Tina Klocke
Chief Financial Bear, Treasurer and Secretary

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Maxine Clark and Tina Klocke, and each of them, his or her true and lawful attorneys-in-fact and agents, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities to sign the Annual Report on Form 10-K of Build-A-Bear Workshop, Inc. (the Company) for the fiscal year ended December 30, 2006 and any other documents and instruments incidental thereto, together with any and all amendments and supplements thereto, to enable the Company to comply with the Securities Act of 1934, as amended, and any rules, regulations and requirements of the Securities and Exchange Commission in respect thereof, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents and/or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Signatures	**Title**	**Date**
/s/ Mary Lou Fiala	Director	March 15, 2007
Mary Lou Fiala		
/s/ James M. Gould	Director	March 15, 2007
James M. Gould		
/s/ Louis M. Mucci	Director	March 15, 2007
Louis M. Mucci		

/s/ William Reisler	Director	March 15, 2007
William Reisler		
/s/ Coleman Peterson	Director	March 15, 2007
Coleman Peterson		

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Signatures	Title	Date
/s/ Joan Ryan Joan Ryan	Director	March 15, 2007
/s/ Maxine Clark Maxine Clark	Chief Executive Bear and Chairman of the Board (Principal Executive Officer)	March 15, 2007
/s/ Tina Klocke Tina Klocke	Chief Financial Bear, Treasurer and Secretary (Principal Financial and Accounting Officer)	March 15, 2007