

**EXHIBIT 13**  
**FINANCIAL STATEMENTS**



**MRS. FIELDS FAMOUS BRANDS, LLC  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE FISCAL YEARS ENDED DECEMBER 31, 2005,  
JANUARY 1, 2005 AND JANUARY 3, 2004**



**KPMG LLP**  
Suite 1500  
15 West South Temple  
Salt Lake City, UT 84101-9901

## **Report of Independent Registered Public Accounting Firm**

The Board of Managers  
Mrs. Fields Famous Brands, LLC:

We have audited the accompanying consolidated balance sheets of Mrs. Fields Famous Brands, LLC (see Note 1) as of December 31, 2005 and January 1, 2005, and the related consolidated statements of operations and comprehensive income (loss), member's deficit and cash flows for the fiscal years ended December 31, 2005, January 1, 2005, and January 3, 2004. In connection with our audits of the consolidated financial statements, we also have audited financial statement schedule II. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

As described in Note 1 to the consolidated financial statements, the accompanying consolidated financial statements prior to formation of the Company on March 16, 2004 were prepared solely to present the assets contributed and the liabilities assumed pursuant to the formation of the Company through the combination of certain assets and liabilities of Mrs. Fields' Original Cookies, Inc. and subsidiaries (MFOC) and all of the assets and liabilities of TCBY Systems, LLC and subsidiaries, and are not intended to be a complete historical presentation of all the assets and liabilities of MFOC.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Mrs. Fields Famous Brands, LLC as of December 31, 2005 and January 1, 2005, and the results of their operations and their cash flows for the fiscal years ended December 31, 2005, January 1, 2005, and January 3, 2004 in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

**KPMG LLP**

Salt Lake City, Utah  
March 17, 2006

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Consolidated Balance Sheets**  
(Dollars in thousands)

	December 31, 2005	January 1, 2005
<b>ASSETS:</b>		
Cash and cash equivalents .....	\$ 23,664	\$ 19,859
Receivables, net of allowance for doubtful accounts of \$612 and \$1,295, respectively .....	8,061	8,039
Amounts due from affiliates .....	-	23
Inventories .....	2,869	2,626
Prepaid expenses and other .....	932	1,200
Deferred tax asset .....	780	1,120
Total current assets .....	36,306	32,867
Property and equipment, net .....	4,360	3,486
Goodwill .....	78,683	113,456
Trademarks and other intangible assets, net .....	12,755	23,419
Deferred loan costs, net of accumulated amortization of \$9,964 and \$9,043, respectively .....	6,964	7,885
Deferred tax asset .....	151	-
Other assets .....	678	668
	\$ 139,897	\$ 181,781
<b>LIABILITIES AND MEMBER'S DEFICIT:</b>		
Accounts payable .....	\$ 6,496	\$ 4,334
Accrued liabilities .....	12,289	14,646
Amounts due to affiliates .....	3,949	2,780
Current portion of capital lease obligations .....	104	36
Current portion of deferred revenues .....	1,074	2,049
Total current liabilities .....	23,912	23,845
Long-term debt .....	195,747	195,747
Capital lease obligations, net of current portion .....	485	427
Deferred revenues, net of current portion .....	1,175	1,387
Deferred tax liability .....	-	3,876
Total liabilities .....	221,319	225,282
Member's deficit .....	(81,273)	(43,365)
Accumulated other comprehensive loss .....	(149)	(136)
Total member's deficit .....	(81,422)	(43,501)
<b>COMMITMENTS AND CONTINGENCIES</b>		
	\$ 139,897	\$ 181,781

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Consolidated Statements of Operations and Comprehensive Income (Loss)**  
(Dollars in thousands)

	For the Fiscal Year Ended		
	December 31, 2005	January 1, 2005	January 3, 2004
<b>REVENUES:</b>			
Franchising .....	\$ 53,528	\$ 55,913	\$ 58,645
Gifts .....	30,136	25,849	17,405
Licensing .....	4,016	4,945	5,464
Other .....	272	353	474
Total revenues .....	<u>87,952</u>	<u>87,060</u>	<u>81,988</u>
<b>OPERATING COSTS AND EXPENSES:</b>			
Franchising .....	21,746	21,893	20,040
Gifts .....	28,418	20,733	13,207
Licensing .....	1,132	1,516	1,155
General and administrative .....	8,527	9,727	10,811
Stock compensation expense .....	-	75	50
Costs associated with debt refinancing, net .....	-	249	684
Depreciation .....	1,145	1,221	1,973
Amortization .....	2,831	2,832	1,780
Impairment of goodwill and intangible assets .....	43,707	-	-
Other operating expenses, net .....	219	147	331
Total operating costs and expenses .....	<u>107,725</u>	<u>58,393</u>	<u>50,031</u>
Income (loss) from operations .....	(19,773)	28,667	31,957
Interest expense, net .....	(20,943)	(24,905)	(25,041)
Other income .....	-	1,054	-
Income (loss) from continuing operations before provision (benefit) for income taxes .....	(40,716)	4,816	6,916
Provision (benefit) for income taxes .....	(2,808)	2,254	2,403
Income (loss) from continuing operations .....	(37,908)	2,562	4,513
Income from discontinued operations (net of income taxes of \$0, \$65 and \$158, respectively) .....	-	104	255
Net income (loss) .....	<u>\$ (37,908)</u>	<u>\$ 2,666</u>	<u>\$ 4,768</u>
<b>COMPREHENSIVE INCOME (LOSS):</b>			
Net income (loss) .....	\$ (37,908)	\$ 2,666	\$ 4,768
Foreign currency translation adjustment .....	(13)	9	(10)
Comprehensive income (loss) .....	<u>\$ (37,921)</u>	<u>\$ 2,675</u>	<u>\$ 4,758</u>

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Consolidated Statements of Member's Deficit**  
(Dollars in thousands)

	Member's Deficit	Deferred Stock Compensation	Accumulated Other Comprehensive Loss	Total
Balance at December 28, 2002 .....	\$ (47,641)	\$ (329)	\$ (135)	\$ (48,105)
Stock compensation expense .....	-	50	-	50
Unvested options returned to plan .....	(204)	204	-	-
Distribution to parent under tax sharing agreement .....	(1,555)	-	-	(1,555)
Other comprehensive loss .....	-	-	(10)	(10)
Net income .....	4,768	-	-	4,768
Other activity with parent .....	(10,969)	-	-	(10,969)
Balance at January 3, 2004 .....	(55,601)	(75)	(145)	(55,821)
Stock compensation expense .....	-	75	-	75
Contribution by parent .....	17,500	-	-	17,500
Repurchase of stock options in parent .....	(108)	-	-	(108)
Other comprehensive income .....	-	-	9	9
Net income .....	2,666	-	-	2,666
Other activity with parent .....	(7,822)	-	-	(7,822)
Balance at January 1, 2005 .....	(43,365)	-	(136)	(43,501)
Other comprehensive loss .....	-	-	(13)	(13)
Net loss .....	(37,908)	-	-	(37,908)
Balance at December 31, 2005 .....	<u>\$ (81,273)</u>	<u>\$ -</u>	<u>\$ (149)</u>	<u>\$ (81,422)</u>

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Consolidated Statements of Cash Flows**  
(Dollars in thousands)

	For the Fiscal Year Ended		
	December 31, 2005	January 1, 2005	January 3, 2004
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income (loss) .....	\$ (37,908)	\$ 2,666	\$ 4,768
Net income from discontinued operations, net of income taxes .....	-	(104)	(255)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Loss on disposal of assets .....	353	-	-
Impairment of goodwill and intangible assets .....	43,707	-	-
Depreciation and amortization .....	3,976	4,053	3,753
Amortization of deferred loan costs .....	921	3,518	4,578
Stock compensation expense .....	-	75	50
Amortization of discount on notes .....	-	1,245	596
Gain on sale of equity warrants .....	-	(1,054)	-
Non-cash debt increases associated with PIK interest .....	-	-	585
Deferred income taxes .....	(3,687)	(523)	(846)
Changes in assets and liabilities:			
Receivables, net .....	(22)	1,031	249
Amounts due to/from affiliates, net .....	1,192	(378)	(4,652)
Inventories, net .....	(243)	(664)	(590)
Prepaid expenses and other .....	268	(78)	(539)
Other assets .....	(111)	(158)	59
Accounts payable .....	2,162	(2,455)	594
Accrued liabilities .....	(2,857)	1,436	6,356
Deferred revenue .....	(1,187)	(872)	(92)
Net cash provided by continuing operating activities .....	6,564	7,738	14,614
Net cash (used in) provided by discontinued operating activities .....	-	(301)	541
Net cash provided by operating activities .....	6,564	7,437	15,155
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Proceeds from sale of equity warrants .....	-	1,054	-
Purchases of property and equipment .....	(2,174)	(859)	(220)
Purchase of license repurchase option .....	(500)	-	-
Net cash (used in) provided by investing activities .....	(2,674)	195	(220)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Net borrowings (payments) under line of credit .....	-	(3,452)	2,480
Principal payments on long-term debt .....	-	(98,014)	(5,609)
Payment of debt financing costs .....	-	(11,975)	(2,351)
Proceeds from issuance of Senior Secured Notes .....	-	115,000	-
Principal payments on capital lease .....	(72)	(37)	-
Contribution by parent .....	-	17,500	-
Repurchase of stock options in parent .....	-	(108)	-
Distribution to parent under tax sharing agreement and merger costs .....	-	-	(76)
Other activity with parent .....	-	(7,996)	(10,969)
Net cash (used in) provided by financing activities .....	(72)	10,918	(16,525)
Effect of foreign exchange rate changes on cash .....	(13)	9	(10)
Net increase (decrease) in cash and cash equivalents .....	3,805	18,559	(1,600)
Cash and cash equivalents at beginning of period .....	19,859	1,300	2,900
Cash and cash equivalents at end of period .....	\$ 23,664	\$ 19,859	\$ 1,300

See accompanying notes to the consolidated financial statements.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Consolidated Statements of Cash Flows (continued)**  
(Dollars in thousands)

	For the Fiscal Year Ended		
	December 31, 2005	January 1, 2005	January 3, 2004
<b>Supplemental Disclosures of Cash Flow Information:</b>			
Cash paid for interest .....	\$ 20,562	\$ 16,541	\$ 19,050
Cash paid for income taxes .....	85	50	317
Cash paid to parent for income taxes .....	-	1,450	7,050
<b>Supplemental Disclosures of Noncash Investing and Financing Activities:</b>			
Assets acquired under capital lease .....	\$ 198	\$ 500	\$ -
Property and equipment contributed by parent .....	-	174	-
Distributions payable to parent under tax sharing agreement .....	-	-	1,555



**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**

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**1. Basis of Presentation and Description of Business**

***Basis of Presentation***

Mrs. Fields Famous Brands, LLC (the "Company" or "Mrs. Fields") is an entity that was formed in March 2004 in connection with the reorganization of certain entities and segments that are under the common control of Mrs. Fields' Companies, Inc. ("MFC"), formerly known as Mrs. Fields' Famous Brands, Inc. The Company is a wholly-owned subsidiary of Mrs. Fields' Original Cookies, Inc., ("MFOC"). MFOC is a wholly-owned subsidiary of Mrs. Fields' Holding Company, Inc. ("MFH"), and MFH is a wholly-owned subsidiary of MFC. Prior to the reorganization, TCBY Systems, LLC ("TCBY") was a wholly-owned subsidiary of TCBY Enterprises, LLC ("TCBY Enterprises"), whose parent was also MFC.

The accompanying consolidated financial statements prior to the formation of the Company on March 16, 2004 include the accounts of TCBY and the franchising, gifts and licensing segments of MFOC. In March 2004, MFC completed a reorganization whereby TCBY and the franchising, gifts and licensing segments of MFOC were contributed to the Company. These financial statements have been prepared to reflect this reorganization as if it had occurred on December 29, 2002 (the beginning of fiscal 2003.)

The consolidated financial statements assume that Mrs. Fields, for all periods presented, had existed as a separate legal entity with the following three business segments: franchising, gifts and licensing. The consolidated financial statements, which have been carved out from the consolidated financial statements of MFOC and TCBY prior to the reorganization using the historical results of operations and assets and liabilities of these businesses and activities and which exclude the company-owned stores segment of MFOC, reflect the accounting policies adopted by MFOC and TCBY in the preparation of their consolidated financial statements and thus do not necessarily reflect the accounting policies which Mrs. Fields might have adopted had it been an independent company. The historical consolidated financial statements of Mrs. Fields include those accounts specifically attributable to Mrs. Fields, substantially all of the indebtedness of MFOC and TCBY, and allocations of expenses relating to shared services and administrative functions incurred at MFOC.

Historically, MFOC has not allocated its various corporate overhead expenses, and common general and administrative expenses to its operating business units. However, an allocation of such expenses has been included in general and administrative expenses for the periods prior to the reorganization in the accompanying consolidated statements of operations and comprehensive income (loss). The Company's general and administrative expenses represent portions of MFOC's corporate functions such as human resources, legal, accounting and finance, treasury and information technology systems, that have been allocated to Mrs. Fields based on percentage of labor hours devoted by the functional department. These allocated costs are not necessarily indicative of the costs that Mrs. Fields would have incurred had it operated as an independent, stand-alone entity for all periods presented.

The other activity with parent line items on the consolidated statements of member's deficit and the consolidated statements of cash flows represent the net activity between the Company and MFOC prior to the reorganization in March 2004.

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles. All transactions and balances between the consolidated entities and segments have been eliminated.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
*(Continued)*

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***Description of Business***

The Company develops and franchises retail stores which sell core products including cookies, brownies, frozen yogurt, ice cream and pretzels through five specialty branded concepts: Mrs. Fields, Great American Cookie Company, TCBY, Pretzel Time and Pretzelmaker.

In connection with its franchising activities, the Company authorizes third-party licensees and franchisees to use certain business formats, systems, methods, procedures, designs, layouts, specifications, trade names and trademarks in the United States of America (the "United States") and other countries. Additionally, the Company licenses the use of its trademarks, logos and recipes to third parties for distribution of Mrs. Fields and TCBY branded products through non-bakery stores and cafes. The Company also markets and distributes products through catalogs and the Internet.

**2. Summary of Significant Accounting Policies**

***Accounting Periods***

The Company operates using a 52/53-week fiscal year ending on the Saturday closest to December 31. Fiscal 2005 and 2004 are 52-week years ending December 31, 2005 and January 1, 2005, respectively. Fiscal 2003 is a 53-week year ending January 3, 2004.

***Foreign Currency Translation***

The balance sheet accounts of foreign subsidiaries are translated into U.S. dollars using the applicable balance sheet date exchange rates, while revenues and expenses are translated using the average exchange rates for the period presented.

***Related-Party Transactions***

Mrs. Fields has contractual relationships with various affiliates, primarily MFOC, MFH, TCBY Enterprises and MFC, which are intended to be fair to the parties involved in the transactions and on terms similar to what could be negotiated with independent third parties. Sometimes the Company is required to negotiate the agreements for both sides of the transaction. Also, inherent in any contractual relationship is the interpretation of the intent of the agreement at a later time when unanticipated events occur. When situations like these occur, the Company attempts objectively to determine the terms of the transaction or interpret the intent of the agreement on a fair and independent basis. However, there is no guarantee that the Company will be successful in doing so. Individual affiliate transactions or a series of related transactions in excess of \$1.0 million require a resolution by the Board of Managers and individual affiliate transactions or a series of related transactions in excess of \$5.0 million require an "opinion of fairness" by an accounting, appraisal or investment banking firm.

***Use of Estimates***

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Company's significant accounting estimates include estimates for employee benefits and related insurances, reserves for doubtful accounts and obsolete and excessive inventories, asset valuation allowances, depreciation and amortization.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
*(Continued)*

***Cash and Cash Equivalents***

Cash and cash equivalents include all cash balances and highly liquid investments with an initial maturity of three months or less. The Company places its temporary cash investments with high credit quality financial institutions. At times such investments may be in excess of the Federal Deposit Insurance Corporation ("FDIC") insurance limit.

***Receivables***

Most of the Company's receivables are due from domestic and international franchisees, distributors, licensees and corporate customers of our gifts segment. These receivables consist of normal trade accounts receivable and longer-term notes receivable. Service charges may be assessed on past due invoices but any revenue associated with these charges is only recognized when collected. The Company maintains an allowance for doubtful accounts to cover potential losses. This allowance is the Company's best estimate of the amount of probable collection losses in the Company's existing trade accounts receivable. The Company determines the allowance based upon historical write-off experience and individual facts and circumstances associated with individual debtors. If the assumptions that are used to determine the allowance for doubtful accounts change, the Company may have to provide for a greater level of expense in future periods or reverse amounts provided in prior periods.

Prior to fiscal 2001, TCBY extended credit from time to time in the form of notes receivable to franchisees and certain of these notes receivable remain outstanding. Notes receivable from franchisees are primarily collateralized by equipment located at the franchisees' stores. These notes bear interest at market rates and mature at various dates through April 2009. TCBY regularly reviews the notes for non-performance. Notes that are considered non-performing are placed on a non-accrual status when the collectability of principal or interest becomes uncertain. During the years ended December 31, 2005, January 1, 2005 and January 3, 2004, TCBY recognized no interest income pertaining to these notes receivable.

Prior to fiscal 2001, TCBY factored various notes receivable aggregating \$2.1 million. Under the terms of the factoring agreement, TCBY is ultimately responsible to the factoring agent for the realizability of the notes receivable. In the event of non-performance, the factoring agent has recourse against TCBY to a maximum level of \$478,000 and \$701,000 as of December 31, 2005 and January 1, 2005, respectively. The Company has reserves of \$478,000 and \$569,000 as of December 31, 2005 and January 1, 2005, respectively, for this potential recourse liability. This reserve is included in accrued liabilities in the accompanying consolidated balance sheets.

Notes receivable at December 31, 2005 and January 1, 2005 comprised the following (in thousands):

	December 31, 2005	January 1, 2005
Non-performing notes .....	\$ -	\$ 521
Allowance for doubtful accounts .....	-	(521)
Non-performing notes, net .....	-	-
Performing notes .....	195	225
Allowance for doubtful accounts .....	(69)	(76)
Performing notes, net .....	126	149
	<u>\$ 126</u>	<u>\$ 149</u>

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
*(Continued)*

The activity in the allowance for notes receivable for the years ended December 31, 2005 and January 1, 2005 is as follows (in thousands):

	December 31, 2005	January 1, 2005
Beginning balance .....	\$ (597)	\$ (713)
Write-offs .....	528	116
	<u>\$ (69)</u>	<u>\$ (597)</u>

***Inventories***

Inventories consist of raw materials, finished goods, packaging and novelties and are stated at the lower of cost (first-in, first-out method) or market value. Inventories at December 31, 2005 and January 1, 2005 are comprised of the following (in thousands):

	December 31, 2005	January 1, 2005
Raw materials .....	\$ 1,283	\$ 958
Finished goods .....	770	643
Packaging .....	548	653
Novelties .....	268	372
	<u>\$ 2,869</u>	<u>\$ 2,626</u>

***Property and Equipment***

Equipment and fixtures are stated at cost less accumulated depreciation and are depreciated over three to seven years using the straight-line method. Leasehold improvements are stated at cost less accumulated depreciation and are depreciated over the term of the lease using the straight-line method. Property and equipment at December 31, 2005 and January 1, 2005 are comprised of the following (in thousands):

	December 31, 2005	January 1, 2005
Leasehold improvements .....	\$ 4,241	\$ 3,879
Equipment and fixtures .....	7,927	9,801
Land .....	240	240
	12,408	13,920
Less accumulated depreciation .....	(8,048)	(10,434)
	<u>\$ 4,360</u>	<u>\$ 3,486</u>

Property and equipment at December 31, 2005 and January 1, 2005 includes gross assets acquired under a capital lease of \$698,000 and \$500,000, respectively, and related accumulated depreciation of \$139,000 and \$53,000, respectively.

Expenditures that materially extend useful lives of property and equipment are capitalized. Routine maintenance, repairs and renewal costs are expensed as incurred. Gains or losses from the sale or retirement of property and equipment are recorded in current operations.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
*(Continued)*

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***Goodwill, Trademarks and Other Intangible Assets***

The Company accounts for goodwill and other intangible assets in accordance with Statement of Financial Accounting Standards ("SFAS") No. 142 ("SFAS 142"), "Goodwill and Other Intangible Assets." Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but are tested for impairment at least annually in accordance with the provisions of SFAS 142. SFAS 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values and be reviewed for impairment in accordance with SFAS No. 144, "Accounting for Impairment or Disposal of Long-Lived Assets."

On an annual basis (in the fourth quarter), the Company performs an assessment for impairment of its carrying value of goodwill associated with each of its reporting units defined as Bakery Franchising, Dairy Franchising, Gifts and Licensing by comparing each reporting unit's fair value with its carrying value. The estimated fair value of goodwill is affected by, among other things, operating results, the Company's business plan for the future, estimated results of future operations and the comparable companies and transactions that are used to estimate the fair value of the goodwill. To the extent that the carrying value of a reporting unit exceeds its fair value, goodwill is written down to its implied fair value. Changes in the business plan or operating results that are different than the projections used to develop the reporting units fair value may have an impact on the valuation of the goodwill. The Company engaged an independent valuation firm to assist us in determining the fair value of each of the Company's reporting units and compared it to the carrying amount of the reporting unit as of December 31, 2005. The carrying amount of the Dairy Franchising reporting unit exceeded its fair value.

The Company compared the implied fair value of the Dairy Franchising reporting unit's goodwill with the carrying amount of the goodwill and determined an impairment of Dairy Franchising goodwill of \$34.8 million for the year ended December 31, 2005. The implied fair value of the goodwill is determined by allocating the fair value of the reporting unit to all of the assets (recognized and unrecognized) and liabilities of the reporting unit in a manner similar to a purchase price allocation, in accordance with SFAS No. 141, "Business Combinations."

Additionally, the Company determined that a triggering event had occurred under SFAS No. 144 as a result of an eroding TCBY franchise system, fewer locations, consistent negative year-over-year same store sales by our TCBY franchisees and the Company's inability to locate and open a significant number of new or additional franchise locations. These factors have resulted in continued decreases in franchise royalties and yogurt formulation revenues from the Company's TCBY franchise system. Therefore, the Company recorded charges to write-down the TCBY trade names and franchise relationships of \$1.7 million and \$7.2 million, respectively, for the year ended December 31, 2005. In addition, the fair value becomes the new basis of the assets and they are amortized over the remaining useful life of the assets pursuant to SFAS No. 144.

The Company anticipates that the TCBY locations will continue to decline in the near future, at least until the reconcepting tests are completed and a plan has been developed to implement the reconcepting in qualified TCBY traditional stores. The Company anticipates the reconcepting tests will be completed in the fourth quarter of fiscal 2006. While management is encouraged by the consumer data we have collected, there can be no assurances that the reconcepting plans or implementation will be successful, or that a reconcepting will slow or reverse the declining TCBY store count or contribution, which may adversely affect the Company's results of operations.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
*(Continued)*

The following outlines the Company's goodwill by reporting unit as of December 31, 2005 and January 1, 2005 (in thousands):

	December 31, 2005	January 1, 2005
Bakery Franchising .....	\$ 60,404	\$ 60,404
Dairy Franchising .....	14,568	49,341
Gifts .....	1,859	1,859
Licensing .....	1,852	1,852
<b>Total .....</b>	<b>\$ 78,683</b>	<b>\$ 113,456</b>

Trademarks and other intangible assets are comprised of definite-lived assets and are amortized over 5 to 15 years. The following outlines the Company's trademarks and other intangibles as of December 31, 2005 and January 1, 2005 (in thousands):

	December 31, 2005	January 1, 2005
Trademarks and trade names .....	\$ 15,404	\$ 19,761
Franchise relationships .....	2,600	13,370
Recipes .....	4,150	4,150
Reacquired franchise and license rights .....	1,528	528
Covenant not to compete .....	-	60
	<u>23,682</u>	<u>37,869</u>
Less accumulated amortization .....	(10,927)	(14,450)
	<u>\$ 12,755</u>	<u>\$ 23,419</u>

During 2005, the Company, through Mrs. Fields Franchising, LLC ("MFF"), entered into an Option Agreement and Amendment to License Agreement (the "Option") with Maxfield Candy Company ("Maxfield"), one of our licensees, who produces and sells Mrs. Fields branded premium candy products in certain distribution channels under a trademark license agreement (the "License"). The Option grants MFF an option to repurchase the License, exercisable during a period from the second to the fifth anniversary of the Option date. The Option purchase price is \$1 million, one-half of which was paid by MFF when the Option was signed by the parties, and one-half of which will be paid to Maxfield on the first anniversary of that date. The repurchase price for the License is due only if MFF exercises the Option and ranges from \$4.5 million to \$7.0 million, depending on when the Option is exercised. One-half of the Option purchase price will be credited to the License repurchase price in a manner described in the Option if MFF exercises the Option. The parties also agreed to certain modifications of the License as part of the Option. At December 31, 2005, the Option purchase price is included in reacquired franchise and license rights and is being amortized over the term of the Option.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
*(Continued)*

Amortization expense of the intangible assets for the years ended December 31, 2005, January 1, 2005 and January 3, 2004 was \$2.7 million, \$2.7 million and \$1.7 million, respectively. Future amortization expense of the intangible assets as of December 31, 2005, is estimated to be as follows (in thousands):

<u>Fiscal Year</u>	
2006 .....	\$ 2,010
2007 .....	1,968
2008 .....	1,968
2009 .....	1,827
2010 .....	1,686
Thereafter .....	3,296
	<u>\$ 12,755</u>

***Deferred Loan Costs***

Deferred loan costs are amortized over the life of the related debt using the effective interest method. During the years ended December 31, 2005, January 1, 2005 and January 3, 2004, the Company amortized deferred loan costs of approximately \$921,000, \$3.5 million and \$4.6 million, respectively, to interest expense.

***Long-Lived Assets***

Long-lived assets are reviewed for impairment when events or changes in circumstances indicate that the book value of an asset may not be fully recovered. The Company uses an estimate of future undiscounted net cash flows of the related asset or group of assets over the remaining life in measuring whether the assets are recoverable. Impairment of long-lived assets is assessed at the lowest level for which there are identifiable cash flows that are independent of other groups of assets. Impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. The impairment of long-lived assets requires judgments and estimates. If circumstances change, such estimates could also change.

***Accrued Liabilities***

Accrued liabilities consist of the following at December 31, 2005 and January 1, 2005 (in thousands):

	<u>December 31,</u> <u>2005</u>	<u>January 1,</u> <u>2005</u>
Accrued liabilities .....	\$ 4,778	\$ 4,701
Accrued compensation and benefits .....	1,534	3,968
Accrued interest payable .....	5,977	5,977
	<u>\$ 12,289</u>	<u>\$ 14,646</u>

On June 24, 2004, the Company announced a reorganization of its executive management team effective June 28, 2004. As a result of this reorganization, the Company terminated the employment of two Senior Vice Presidents effective June 28, 2004 and accrued approximately \$600,000 related to severance expenses. As of December 31, 2005, there were no remaining severance payments. As of January 1, 2005, remaining severance payments of \$466,000 were included in accrued compensation and benefits.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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On May 7, 2003, the Board of Directors of MFOC accepted the resignation of Larry A. Hodges as its President, Chief Executive Officer and Director, which resignation was effective on May 14, 2003. Pursuant to the terms of a Separation Agreement dated August 6, 2003 and a Severance Assumption Agreement dated March 16, 2004 among MFC, MFOC, the Company and Mr. Hodges (the "Separation Agreements"), Mr. Hodges received 28 months of salary as severance, which was paid semi-monthly through the end of 2004, and the balance was paid in a lump sum in January 2005. An aggregate of \$321,000 in severance payments were due to Mr. Hodges and were included in accrued compensation and benefits as of January 1, 2005.

***Revenue Recognition***

Initial franchising and licensing fees are recognized when all material services or conditions relating to the franchising or licensing have been substantially performed or satisfied, which is generally upon the opening of a store by a franchisee or licensee. Franchise and license royalties, which are based on a percentage of gross store sales, are recognized as earned, which is generally upon sale of product by franchisees or licensees. Minimum royalty payments under certain licensing agreements are deferred and recognized on a straight-line basis over the term of the agreement. Revenues from the sale of cookie dough that the Company produces and sells to certain franchisees are recognized at the time of shipment and are classified in franchising revenues. Revenues from the sale of cookie dough to grocery stores and wholesale clubs are recognized upon shipment and are included in other revenues. Revenues from gifts are recognized at the time of shipment.

The Company receives cash payments for product formulation fees and allowances from suppliers based on the amount of product purchased directly by our distributors and franchisees. The product formulation fees include cash payments to the Company for the right to use the Company's proprietary formulations and recipes to manufacture the frozen dough, dough mixes and TCBY products these suppliers sell to our franchisees. Formulation fees and allowances are recorded as franchising revenues upon shipment of product to the Company's distributors or franchisees. During fiscal 2005, 2004 and 2003, we included in franchising revenues \$12.8 million, \$15.1 million and \$16.5 million, respectively, for product formulation fees and allowances.

In March 2003, the Company received \$2.0 million from a supplier as an advance to maintain and expand beverage concepts at the Company's franchised store locations. This advance is being recognized as franchising revenues on a ratable basis over the six-year term of the agreement.

***Operating Expenses***

Franchising operating expenses consist of costs incurred to generate franchising revenues which include (i) franchise development and support expenses including expenses relating to brand investment initiatives; (ii) operations and supervision expenses; and (iii) product cost of sales of our manufacturing facility.

Gifts operating expenses consist of costs incurred to generate gift revenues which include (i) cost of sales; (ii) selling and advertising costs; and (iii) general and administrative expenses directly related to the gifts segment. Cost of sales includes inbound freight charges, purchasing and receiving costs, inspection costs, warehousing costs and other costs of our distribution network.

Licensing operating expenses consist of costs incurred to generate licensing revenues, which primarily are selling expenses, which include (i) payroll and payroll-related costs; (ii) outside commissions; and (iii) professional fees.



**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
*(Continued)*

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General and administrative expenses include (i) payroll and payroll-related costs of corporate employees such as executive, accounting, legal, human resources and information systems personnel; (ii) travel and travel-related expenses of corporate employees; (iii) professional and legal fees, bank charges, insurance costs and facility costs not related to the generation of revenues. These costs are associated with providing management support for all of our business segments.

***Shipping and Handling Costs***

The Company charges its gifts and manufacturing facility customers for shipping and handling costs and records the revenues in gifts revenues and franchising revenues, respectively. The costs for shipping and handling are included in gifts expense and franchising expense, respectively.

***Income Taxes***

The Company is organized as a single-member limited liability company and will not elect to be taxed as a corporation for federal income tax purposes. As such, for federal income tax purposes, the Company will be "disregarded" and will be treated as a division of MFOC, its sole member. Although the Company is not expected to be a tax-paying entity, the assets of the Company could be subject to income tax claims against any member of its parent's consolidated group.

The Company will be included in the consolidated federal income tax return of MFC, the Company's ultimate parent. For historical financial reporting purposes, the Company has recognized income tax expense and deferred tax assets and liabilities as if it were filing a separate tax return. The Company has recognized deferred tax assets or liabilities for expected future tax consequences of events that have been recognized in the financial statements or tax returns. Under this method, deferred tax assets or liabilities have been determined based upon the difference between the financial and income tax bases of assets and liabilities using enacted tax rates expected to apply when differences are expected to be settled or realized.

***Fair Value of Financial Instruments***

The Company estimates that the total fair market value of its 9 percent Senior Secured Notes (see Note 3) and its 11½ percent Senior Secured Notes (see Note 3) was approximately \$56.5 million and \$92.0 million, respectively, as of December 31, 2005. These estimates are based on quoted market prices. The book values of the Company's other financial instruments, including accounts receivable and accounts payable, approximate fair values at the respective balance sheet dates because of the relatively short maturity of these instruments or valuation allowances which have been recorded to report the balances at fair value. The carrying amount of other long-term debt obligations approximates its fair value because the related interest rates are at market rates.

***Advertising***

The Company administers advertising funds collected from its franchisees. The Company directs the expenditures of the advertising funds in connection with advertising and marketing campaigns for the benefit of the respective concepts. The advertising funds and their related activities are not included in the accompanying consolidated financial statements.

Advertising costs are expensed as incurred. During the years ended December 31, 2005, January 1, 2005, and January 3, 2004, the Company incurred advertising expenses excluding the expenditures of the advertising funds totaling approximately \$6.0 million, \$4.5 million and \$1.7 million, respectively.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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***Recent Accounting Pronouncements***

In May 2005, the Financial Accounting Standards Board ("FASB") issued SFAS No. 154 ("SFAS 154"), "Accounting for Changes and Errors Corrections - a Replacement of APB Opinion 20 and FASB Statement No. 3." Previously, Accounting Principles Board Opinion No. 20 ("APB 20"), "Accounting Changes" and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements" required the inclusion of the cumulative effect of changes in accounting principles in net income of the period of the change. SFAS 154 requires companies to recognize changes in accounting principles, including changes required by new accounting pronouncements when the pronouncement does not include specific transition provisions, retrospectively to prior periods' financial statements. The Company will assess the impact of a retrospective application of a change in accounting principle in accordance with SFAS 154 if the need for such a change arises after the effective date of January 1, 2006.

In December 2004, the FASB issued SFAS No. 123 (revised 2004) ("SFAS 123R"), "Share-Based Payment," which is a revision of SFAS No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation." SFAS 123R supersedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees". Generally, the approach in SFAS 123R is similar to the approach described in SFAS 123. However, SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based upon their fair values. Pro forma disclosure is no longer an alternative. The new standard will be effective for the Company beginning January 1, 2006. The adoption of SFAS 123R is not expected to have a material impact on the Company's consolidated financial position or results of operations.

In November 2004, the FASB issued SFAS No. 151 ("SFAS 151"), "Inventory Costs, an amendment of ARB No. 43, Chapter 4," which clarifies the types of costs that should be expensed rather than capitalized as inventory. This statement also clarifies the circumstances under which fixed overhead costs associated with operating facilities involved in inventory processing should be capitalized. The new standard will be effective for the Company beginning January 1, 2006. The adoption of SFAS 151 is not expected to have a material impact on the Company's consolidated financial position or results of operations.

**3. Long-Term Debt and Capital Lease Obligations**

***Long-Term Debt***

Long-term debt consists of the following at December 31, 2005 and January 1, 2005 (in thousands):

	<u>December 31, 2005</u>	<u>January 1, 2005</u>
Senior Secured Notes, interest at 11 1/2 percent payable semi-annually in arrears on March 15 and September 15, due March 15, 2011 .....	\$ 115,000	\$ 115,000
Senior Secured Notes, interest at 9 percent payable semi-annually in arrears on March 15 and September 15, due March 15, 2011 .....	80,747	80,747
	<u>\$ 195,747</u>	<u>\$ 195,747</u>

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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***Debt Refinancing***

On March 16, 2004, the Company issued \$80.7 million of 9 percent senior secured notes (the "9 percent Senior Secured Notes") in exchange for \$80.7 million of existing senior notes (the "Senior Notes") and issued \$115.0 million of 11½ percent senior secured notes (the "11½ percent Senior Secured Notes" together with the 9 percent Senior Secured Notes, the "Senior Secured Notes"). The proceeds from the 11½ percent Senior Secured Notes were used to retire substantially all of the Company's indebtedness, except capital lease obligations.

The Senior Secured Notes will mature March 15, 2011, with interest payable semi-annually. The Senior Secured Notes rank senior in right of payment to all subordinated indebtedness of the Company and rank equal in right of payment with all existing and future senior indebtedness of the Company. The Senior Secured Notes are secured by all of the tangible and intangible assets of the Company and its subsidiaries.

The Senior Secured Notes are redeemable at the option of the Company anytime on or after March 15, 2008. The Company may redeem up to 35 percent of the aggregate principal amount of the notes with the net proceeds of certain equity offerings prior to March 15, 2007. The Senior Secured Notes require the Company to offer to repurchase a portion of the notes at 100 percent of the principal amount, plus accrued and unpaid interest thereon to the date of purchase, with 50 percent of the Company's "excess cash flow", as defined in the indenture agreement, when the ratio of the Company's Net Indebtedness to Consolidated EBITDA is above 3.75 to 1.0 and the cumulative unpaid excess cash flow offer amount exceeds \$10.0 million. In the event of a change in control, the holders of the Senior Secured Notes will have the right to put the notes to the Company at 101 percent of their principal amount, plus accrued and unpaid interest, provided at least 65 percent of the aggregate principal amount of the Senior Secured Notes originally issued remain outstanding.

The Senior Secured Notes contain certain covenants that limit among other things, the ability of the Company and its subsidiaries to (i) incur additional indebtedness; (ii) make certain investments or enter into sale and leaseback transactions; (iii) pay dividends, redeem subordinated debt, repurchase the Company's or its subsidiaries stock or make any other restricted payments as defined in the indenture; (iv) enter into certain transactions with affiliates; (v) create or incur liens; (vi) transfer or sell assets; (vii) make dividends, distributions or other payments from the Company's subsidiaries; (viii) consummate a merger, consolidation or sale of all or substantially all of our assets; and (ix) engage in unrelated business.

As of January 1, 2005, the Company had incurred \$13.9 million of costs directly related to the debt refinancing. Generally, these costs would be deferred and amortized as interest expense over the term of the Senior Secured Notes. However, for the years ended January 1, 2005 and January 3, 2004, respectively, approximately \$5.0 million and \$684,000 of these costs related to the exchange of \$80.7 million of Senior Notes for \$80.7 million of Senior Secured Notes and were expensed, net of the gain recognized on the early retirement of the remaining indebtedness of \$4.8 million during the year ended January 1, 2005, in the respective period in accordance with SFAS No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings" and included in the caption "costs associated with debt refinancing, net" in the consolidated statements of operations.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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**Capital Lease Obligations**

As of December 31, 2005, the future minimum lease payments, including interest, for capital lease obligations are as follows (in thousands):

<u>Fiscal Year</u>		
2006 .....	\$	158
2007 .....		158
2008 .....		116
2009 .....		85
2010 .....		85
Thereafter .....		199
Total minimum lease payments .....		<u>801</u>
Less amount representing interest .....		<u>(212)</u>
Present value of net minimum lease payments .....	\$	<u>589</u>

**4. Income Taxes**

**Provision for Income Taxes**

The components of the provision for income taxes for the years ended December 31, 2005 January 1, 2005 and January 3, 2004 are as follows (in thousands):

	<u>For the Fiscal Year Ended</u>		
	<u>December 31,</u> <u>2005</u>	<u>January 1,</u> <u>2005</u>	<u>January 3,</u> <u>2004</u>
Current			
Federal .....	\$ 693	\$ 2,180	\$ 2,697
State .....	150	517	552
Foreign .....	36	80	-
	<u>879</u>	<u>2,777</u>	<u>3,249</u>
Deferred			
Federal .....	(3,061)	(434)	(670)
State .....	(626)	(89)	(176)
	<u>(3,687)</u>	<u>(523)</u>	<u>(846)</u>
Total provision (benefit) for income taxes	<u>\$ (2,808)</u>	<u>\$ 2,254</u>	<u>\$ 2,403</u>

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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The differences between income taxes at the U.S. federal statutory income tax rate and income taxes reported in the consolidated statements of operations for the years ended December 31, 2005, January 1, 2005 and January 3, 2004 are as follows (in thousands):

	For the Fiscal Year Ended		
	December 31, 2005	January 1, 2005	January 3, 2004
Federal statutory income tax rate .....	\$ (13,843)	\$ 1,637	\$ 2,299
State income taxes .....	(315)	209	269
Impairment of goodwill and intangibles .....	11,301	-	-
Foreign taxes .....	-	80	-
Deferred compensation adjustment .....	-	572	-
Other .....	49	(244)	(165)
Effective income tax rate .....	<u>\$ (2,808)</u>	<u>\$ 2,254</u>	<u>\$ 2,403</u>

The significant components of the Company's deferred tax assets and liabilities at December 31, 2005 and January 1, 2005 are as follows (in thousands):

	December 31, 2005	January 1, 2005
Deferred tax assets - current:		
Allowance for doubtful accounts .....	\$ 232	\$ 411
Deferred revenues .....	52	198
Accrued expenses .....	304	407
Other .....	192	104
Deferred tax assets - current: .....	<u>\$ 780</u>	<u>\$ 1,120</u>
Deferred tax liabilities - long-term:		
Intangibles .....	\$ (2,084)	\$ (6,682)
Other .....	(95)	(134)
Total deferred tax liabilities - long-term .....	<u>(2,179)</u>	<u>(6,816)</u>
Deferred tax assets - long-term:		
Loan costs .....	1,575	1,888
Reserves .....	23	391
Depreciation .....	455	350
Other .....	277	311
Total deferred tax assets - long-term .....	<u>2,330</u>	<u>2,940</u>
Deferred tax asset (liability), net - long-term .....	<u>\$ 151</u>	<u>\$ (3,876)</u>

A valuation allowance is provided when it is more likely than not that all or some of the deferred income tax assets will not be realized. Management has concluded that it is more likely than not that the Company will realize its deferred income tax assets.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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In connection with the reorganization described in Note 1, the Company entered into a tax allocation agreement with MFC pursuant to which the Company agreed to make payments to MFC, after taking into account payments the Company makes directly to tax authorities, based on the Company's stand-alone consolidated federal income tax liability, determined as if the Company and its subsidiaries constituted their own consolidated group for federal income tax purposes. The Company will not be permitted to make these payments to MFC, unless the MFC federal tax liability exceeds the Company's stand-alone federal tax liability, until it meets certain financial ratios and is otherwise in compliance with the terms of the indenture governing the Senior Secured Notes.

**5. Long-Term Incentive Plans**

Effective as of May 23, 2004, the Board of Directors of MFC approved adoption of the Phantom Stock Plan of Mrs. Fields' Companies, Inc. (the "Phantom Plan"). The purpose of the Phantom Plan is to provide long-term incentives to key employees of MFC or its subsidiaries (the "Participants") as determined by the Compensation Committee of the Board of Directors (the "Committee"). The Phantom Plan is unfunded, and Participants do not receive any payment under the Phantom Plan until the completion of the first to occur of (i) a sale of substantially all of the assets of MFC; (ii) a public offering of MFC's Common Stock where MFC receives proceeds, net of any underwriter's discounts and expenses, of not less than \$50 million; or (iii) any stock sale, merger or other transaction where the owners of Common Stock immediately before the transaction do not own in excess of 50 percent of the common stock of the entity surviving such sale, merger or other transaction (a "Triggering Event").

Participants receive performance units in amounts recommended by the CEO and determined by the Committee. Upon the completion of a Triggering Event, Participants receive payments reflecting the number and value of their performance units at the time of the completion of the Triggering Event. Payments to Participants may be made in cash or through issuance of equity securities of MFC, as determined by the Committee, at which time compensation expense will be recognized. The value of a performance unit at the completion of a Triggering Event is the value of one share of common stock of MFC as determined in good faith by the Board of Directors. If the Board of Directors determines the need, it may seek the advice of an independent advisor.

The maximum number of performance units that may be granted under the Phantom Plan is one million units. Subdivisions, splits, or combinations involving MFC's Common Stock will proportionately affect the number of performance units that have been awarded under the Phantom Plan. In May 2004, the Committee approved the grant of up to 392,418 performance units allocated among Participants as determined by the Committee. Future grants, if any, shall also be determined by the Committee. As of December 31, 2005, 341,400 performance units have been granted to Participants.

Effective as of September 1, 2004, MFC terminated its Employee Stock Option Plan pursuant to the provisions of the plan. No further options will be granted under the plan. Valid and outstanding options granted to plan participants prior to termination were unaffected by the termination. Concurrent with the termination, the Company paid \$108,000 for the repurchase of certain stock options from the plan participants. Concurrent with the issuance of the performance units of the Phantom Plan, most of the outstanding stock options were cancelled. At December 31, 2005, there are 10,000 stock options outstanding.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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During the years ended January 1, 2005 and January 3, 2004, the Company recognized \$75,000 and \$50,000 of compensation expense, respectively, related to the fiscal 2001 issuance of MFC stock options to certain employees of the Company. Because the employees of the Company are the beneficiaries of the grant of options in MFC stock, the related expense has been reflected in the Company's consolidated financial statements.

**6. Commitments and Contingencies**

***Legal Matters***

The Company and its products are subject to regulation by numerous governmental authorities, including without limitation, federal, state and local laws and regulations governing franchising, health, sanitation, environmental protection, safety and hiring and employment practices.

In the ordinary course of business, the Company is involved in routine litigation, including franchise disputes and trademark disputes. The Company is not a party to any legal proceedings (including the matter described below) which, in the opinion of management, after consultation with legal counsel, is material to its business, financial condition or results of operations.

Effective as of August 13, 2005, the Company's wholly-owned subsidiary, MFF, terminated two license agreements (the "License Agreements") with Shadewell Grove IP, LLC ("Shadewell") for Shadewell's failure to make certain payments to MFF in a timely manner. These terminated License Agreements granted Shadewell a license to develop, manufacture, distribute and sell ready-to-eat shelf stable cookie products and high quality, prepackaged, ready-to-eat, pre-baked cookie products using certain Mrs. Fields trademarks, service marks and trade names in distribution channels designated in the License Agreements.

On October 5, 2005, Shadewell filed a Verified Complaint, Motion for Restraining Order and related documents (the "Action") in the Court of Chancery of the State of Delaware against MFF. In the Action, Shadewell alleges that they did not materially breach the shelf-stable and ready-to-eat, pre-baked cookie licenses, and that the License Agreements were improperly terminated by MFF. Among other relief, Shadewell seeks a court order that the License Agreements remain in full force and effect and that MFF must specifically perform its obligations under the License Agreements. Shadewell also seeks unspecified damages related to its claims that MFF breached certain obligations under the License Agreements. A trial of the Action was held on November 29, 2005, followed by post-trial briefs and arguments in January 2006, but the court has not yet rendered its decision. The Company believes that Shadewell's allegations in the Action are without merit and intends to vigorously defend its interests. The Company believes that neither the Action nor the termination of the License Agreements will have a material effect on the Company's consolidated financial position or results of operations. During 2005, royalties earned from the terminated licenses totaled \$2.2 million.

***Operating Leases***

The Company leases office space, facilities and equipment under long-term non-cancelable operating lease agreements with remaining terms of one to eight years. Rent expense, net of sublease payments, was \$1.3 million, \$1.2 million and \$1.2 million for the years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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As of December 31, 2005, the future minimum lease payments due under operating leases are as follows (in thousands):

<u>Fiscal Year</u>		
2006 .....	\$	1,617
2007 .....		1,547
2008 .....		1,499
2009 .....		1,486
2010 .....		1,505
Thereafter .....		670
	<u>\$</u>	<u>8,324</u>

As of December 31, 2005, the future minimum sublease payments due to the Company under these operating leases are as follows (in thousands):

<u>Fiscal Year</u>		
2006 .....	\$	253
2007 .....		163
2008 .....		123
2009 .....		39
	<u>\$</u>	<u>578</u>

***Contractual Arrangements***

The Company has entered into supply agreements to purchase frozen dough products, yogurt-based products, novelties and ice cream. The frozen dough product supply agreement stipulates minimum annual purchase commitments of not less than 15 million pounds of products, approximately \$19.7 million based on weighted average prices in effect December 31, 2005, each year through the end of the contract, December 2006. These annual purchase commitments are satisfied primarily through the direct purchase of frozen dough products by franchisees. Should the Company not meet the annual minimum commitment, the supplier's sole remedy is to cancel the supply agreement. The Company did not meet the annual minimum purchase commitment for the year ended December 31, 2005; however, management does not expect the supplier to cancel the supply agreement.

The supplier of the frozen dough product manufactures its products in one location. A production disruption or the supplier's inability to secure the raw materials used in the production of its products could adversely affect the operating results of the Company and its franchisees. Although management believes that other suppliers could provide similar products on comparable terms, a change in suppliers could cause a delay in manufacturing and a possible loss of sales, which could adversely affect the financial position, results of operations or liquidity of the Company and its franchisees.



**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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TCBY's supply agreement with Americana Foods Limited Partnership ("Americana") for the purchase of yogurt-based products, novelties and ice cream (the "TCBY Supply Agreement") stipulates minimum annual purchase commitments of at least 75 percent of the product volumes contained in the agreement through the term of the agreement, November 2007. These annual purchase commitments are satisfied through the direct purchase of frozen yogurt-based products, novelties and ice cream by TCBY's distributors and franchisees. If the purchases fall below 75 percent of the quantity, then Americana has the right to propose a new pricing structure. If TCBY doesn't agree to the new pricing structure, then Americana has the right to terminate the agreement by giving written notice 180 days prior to termination. The Company did not meet the minimum annual purchase commitment for the year ended December 31, 2005; however, management does not expect Americana to propose a new pricing structure.

Americana manufactures its products in one location. A production disruption or Americana's inability to secure the raw materials used in the production of its products could adversely affect the operating results of TCBY and its franchisees. Although management believes that other suppliers could provide similar products on comparable terms, a change in suppliers could cause a delay in manufacturing and a possible loss of sales, which could adversely affect the financial position, results of operations or liquidity of TCBY and its franchisees.

**7. Related-Party Transactions**

***Due To/From Affiliates***

The amounts due to/from affiliates are comprised of amounts due to/from MFOC, MFH, TCBY Enterprises and affiliates and MFC at December 31, 2005 and January 1, 2005 (in thousands):

	<u>December 31,</u> <u>2005</u>	<u>January 1,</u> <u>2005</u>
Amounts due from affiliates:		
MFC .....	\$ -	\$ 23
Amounts due to affiliates:		
MFC - tax sharing .....	\$ 3,138	\$ 2,382
MFH .....	273	273
MFOC .....	538	125
	<u>\$ 3,949</u>	<u>\$ 2,780</u>

The Company has from time-to-time engaged Korn/Ferry International ("Korn/Ferry"), an international executive recruiting firm for which Richard Ferry, one of the members of the board of managers, is also Founder Chairman. For the years ended December 31, 2005, January 1, 2005 and January 3, 2004, recruiting fees paid to Korn/Ferry totaled \$158,000, \$132,000 and \$362,000, respectively.

The Company has periodically engaged Applied Predictive Technologies ("APT") to evaluate the economic and demographic trends of certain mall and retail site locations. Walker Lewis, one of the members of the board of managers, is Chairman of the Board of APT. For the year ended January 3, 2004, the Company paid APT \$68,000. There were no amounts paid to APT in fiscal 2005 or 2004.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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***Franchise Agreements with MFOC***

Concurrent with the completion of the reorganization (see Note 1), certain of the Company's brand franchisor subsidiaries entered into franchise agreements with MFOC, which permit MFOC to sell and distribute the Company's products in its owned stores upon payment of franchise royalties and other amounts required under the franchise agreements. These franchise agreements are similar to the Company's standard form of franchise agreement, except that the Company did not charge an up-front franchising fee for stores open as of the date of the franchise agreements in recognition of the fact that the stores owned and operated by MFOC were operated prior to giving effect to the reorganization.

These franchise agreements are terminable by the Company in the event of non-payment of the franchise royalties for a period of 10 days, followed by a 10-day opportunity to cure, or other material violation of the franchise agreements. The aggregate amount of franchise royalties paid to the Company by MFOC during fiscal 2005 and 2004 was \$689,000 and \$2.8 million, respectively. The aggregate amount of franchise royalties that would have been required to be paid to the Company by MFOC, had these franchise agreements been in effect, would have been \$4.8 million for fiscal 2003.

***Management Agreement with MFOC***

In connection with the reorganization (see Note 1), the Company entered into a management agreement with MFOC, pursuant to which the Company provides business and organizational strategy, financial and investment management and other executive-level management services to MFOC and its subsidiaries (other than the Company) upon the terms and conditions set forth in the management agreement. As compensation for these services, on a monthly basis, MFOC reimburses the Company the allocated costs of the general and administrative functions dedicated to providing these services as determined in good faith by the Company and MFOC. These reimbursement amounts are intended to reflect the actual costs of providing these services and are not intended to generate revenues for the Company. Management expects that the reimbursement amounts will decrease over time as MFOC reduces its store operations. It is intended that this management agreement will continue in effect until the expiration of all store leases for which MFOC is the lessee. For the year ended December 31, 2005 and the period from the reorganization through January 1, 2005, MFOC reimbursed the Company \$2.4 million and \$2.8 million, respectively, for management services provided under the management agreement.

***MFOC Sublease***

Concurrent with the completion of the reorganization (see Note 1), the Company entered into an assignment agreement whereby the lease for the corporate headquarters was assigned from MFOC to the Company. MFOC entered into a sublease with the Company to pay the Company, over the term of the sublease, agreed rental payments that have been established based on estimated usage of the headquarters by their personnel. For the year ended December 31, 2005 and the period from the reorganization through January 1, 2005, MFOC paid rent of \$289,000 and \$220,000, respectively, to the Company. Management estimates that MFOC's aggregate rental payments will be approximately \$88,000 in fiscal 2006. MFOC's share is expected to decrease over time with corresponding reduced operations. It is intended that the sublease will continue in effect until the expiration of all store leases for which MFOC is the lessee, following which the MFOC sublease will be terminated and the Company would therefore be responsible for all rental payments.

***MFOC Collection Agency Agreement***

Concurrent with the completion of the reorganization (see Note 1), the Company entered into a collection agency agreement with MFOC under which the Company agreed to act as MFOC's collection agent for subtenant rental payments made by the Company's franchisees who operate stores previously owned by MFOC on which MFOC remains as the tenant.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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***Benefits Agreement with MFOC***

Concurrent with the completion of the reorganization (see Note 1), the Company entered into a benefits agreement with MFOC under which the Company agreed to make certain payments to MFOC in respect to the Company's share of employee benefits costs based on the number of the Company's employees. Costs associated with the Company's employees providing services to MFOC under the management agreement are allocated consistent with the shared expenses under the management agreement. For the year ended December 31, 2005 and the period from the reorganization through January 1, 2005, the Company paid MFOC \$2.9 million and \$1.9 million, respectively, for the Company's share of employee benefits costs.

***Insurance Allocation Agreement with MFC***

Concurrent with the completion of the reorganization (see Note 1), the Company entered into an insurance allocation agreement with MFC under which the Company agreed to make certain payments to MFC in respect to the Company's share of certain insurance costs, allocated based on the Company's estimation of the appropriate risk of loss of each of MFC's subsidiaries. The insurance allocation agreement also provides for the allocation of workers' compensation costs based on the respective employee payroll and employment category risk factor of each of MFC's subsidiaries that generates payroll. For the year ended December 31, 2005 and the period from the reorganization through January 1, 2005, the Company paid MFC \$1.3 million and \$925,000, respectively, for the Company's share of insurance costs.

***Shadewell Grove Holdings, LLC and Shadewell Grove IP, LLC***

Prior to 2004, the Company had entered into various trademark license agreements and exclusively licensed certain recipes to Nonni's Food Company, Inc. ("Nonni's"), a manufacturer and distributor of soft baked cookies. In addition, the Company owned warrants to purchase 111,111 shares of Nonni's common stock at an exercise price of \$10.775. In March 2004, Nonni's was acquired by a third party investor in a stock purchase (the "Nonni's Purchase"). As part of the Nonni's Purchase, in consideration for the sale of the warrants to purchase 111,111 shares of Nonni's common stock, the Company was to receive an aggregate of \$1.3 million, of which approximately \$200,000 was being held in an escrow account pending post-closing adjustments related to the Nonni's Purchase. As a result, the Company recorded a gain on the sale of these warrants of \$1.1 million in other income in the consolidated statement of operations during the year ended January 1, 2005. The Company received \$122,000 in January 2006 from Nonni's as final settlement related to the amount previously held in escrow and will record a gain on the sale of the warrants in other income in the consolidated statement of operations during the first quarter of fiscal 2006.

Immediately prior to the Nonni's Purchase, the Mrs. Fields product division of Nonni's and its related assets were contributed to a newly-formed entity, Shadewell Grove Holdings, LLC ("Shadewell Holdings"). The Company received from Shadewell Holdings its pro-rata share of preferred units in Shadewell Holdings, approximately 4.1 percent, as if the warrants in Nonni's common stock had been exercised immediately prior the Nonni's purchase.

In March 2005 and December 2004, the Company paid Shadewell Holdings approximately \$48,000 and \$102,000, respectively, for additional preferred units of Shadewell Holdings to maintain its pro-rata ownership of Shadewell Holdings. This investment is recorded in other assets in the consolidated balance sheet as of December 31, 2005 and January 1, 2005. The Company has appointed John Lauck, one of its executive officers, to represent the Company as a director of Shadewell Holdings.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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Shadewell, a wholly-owned subsidiary of Shadewell Holdings, has licenses to develop, manufacture and distribute ready-to-eat shelf stable cookie products utilizing the Mrs. Fields trademarks, service marks and trade names through retail distribution channels and designated food service distribution channels. Shadewell also has a license to market and distribute high quality, pre-packaged chocolate chips utilizing the Mrs. Fields trademarks, service marks and trade names through designated retail distribution channels. For the years ended December 31, 2005, January 1, 2005, and January 3, 2004, the Company earned royalty and licensing revenues associated with the licensing and recipe sales agreements of \$2.3 million, \$3.1 million and \$3.5 million, respectively.

On December 24, 2004, the Company terminated the license agreement with Shadewell to market and distribute high quality, frozen cookie dough products utilizing the Mrs. Fields trademarks, service marks and trade names to the food away from home industry through designated food service distribution channels. Among other reasons, the Company pursued the termination of this license to better align the Company's interests with those of the Company's franchisees. The Company paid Shadewell a termination fee of \$1.1 million and in return received from Shadewell an indemnification and release of any and all claims arising from the license agreement. The termination fee was recorded in licensing expenses in the consolidated statement of operations for the year ended January 1, 2005.

***Co-marketing and Supply Agreement***

Americana is owned by an entity in which a limited partner of the entity is a subsidiary of a significant shareholder of MFC. Americana manufactures yogurt-based products, ice cream and novelty items for sale and distribution to TCBY's franchisees and distributors under the TCBY Supply Agreement dated November 20, 2002 (see Note 6). Under the TCBY Supply Agreement, the Company recognized revenues related to the product manufactured by Americana of \$9.6 million, \$11.7 million and \$13.1 million for the years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively. In addition, Americana sells TCBY branded frozen specialty products and private label products through retail channels and pays TCBY a portion of the sales price under the TCBY Supply Agreement. TCBY invoiced Americana \$711,000, \$930,000 and \$1.9 million for the fiscal years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively, relating to TCBY's portion of these sales. As a result of these sales, TCBY must reimburse Americana for certain costs. Americana invoiced TCBY \$180,000, \$381,000 and \$892,000 for the fiscal years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively, relating to the reimbursement of these costs.

**8. Employee Benefit Plans**

MFOC sponsors the Mrs. Fields' Original Cookies, Inc. 401(k) Retirement Savings Plan (the "Plan") for all eligible employees of MFOC and its subsidiaries. Under the terms of the Plan, employees may make contributions to the Plan. During 2005 and 2004, a portion of the employee contributions to the Plan were matched by contributions from the Company at the rate of 100 percent of the first three percent of employee contributions plus 50 percent of the next two percent of employee contributions. The total matching contributions made by the Company to the Plan for the years ended December 31, 2005 and January 1, 2005 were approximately \$349,000 and \$294,000, respectively. No contributions were made to the Plan by the Company for the year ended January 3, 2004.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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**9. Reportable Segments**

Operating segments are components of the Company for which separate financial information is available that is evaluated regularly by management in deciding how to allocate resources and in assessing performance. This information is reported on the basis that it is used internally for evaluating segment performance. The Company has three reportable operating segments; namely, franchising, gifts and licensing. The franchising segment consists of revenues received either directly or indirectly from cookie, yogurt and pretzel stores, which are owned and operated by third parties. These revenues include initial franchise or license fees, monthly royalties based on a percentage of a franchisee's gross sales, sales of cookie dough that the Company produces and certain product formulation fees and supplier allowances which are based upon sales to franchisees. The gifts segment includes sales generated from the Company's mail order gift catalog and website. The licensing segment consists of other licensing activity from third parties for the sale of products bearing the Company's brand names. The accounting policies for the segments are the same as those discussed in the summary of significant accounting policies (see Note 2). Sales and transfers between segments are eliminated in consolidation.

The Company evaluates performance of each segment based on contribution. Contribution is computed as the difference between the revenues generated by a reportable segment and the selling and occupancy expenses, cost of sales and direct general and administrative expenses related to that reportable segment. Contribution is used as a measure of the operating performance of an operating segment. The Company does not allocate any indirect general and administrative expense, other operating income (expense), interest expense, depreciation and amortization or assets to its reportable operating segments.

Segment revenues and contribution for the years ended December 31, 2005, January 1, 2005 and January 3, 2004 are presented in the following table (in thousands):

<u>Total Company</u>	<u>For the Fiscal Year Ended</u>		
	<u>December 31, 2005</u>	<u>January 1, 2005</u>	<u>January 3, 2004</u>
<b>Revenues:</b>			
Franchising .....	\$ 53,528	\$ 55,913	\$ 58,645
Gifts .....	30,136	25,849	17,405
Licensing .....	4,016	4,945	5,464
	<u>\$ 87,680</u>	<u>\$ 86,707</u>	<u>\$ 81,514</u>
<b>Contribution:</b>			
Franchising .....	\$ 31,782	\$ 34,020	\$ 38,605
Gifts .....	1,718	5,116	4,198
Licensing .....	2,884	3,429	4,309
	<u>\$ 36,384</u>	<u>\$ 42,565</u>	<u>\$ 47,112</u>

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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The reconciliation of contribution to net income for the years ended December 31, 2005, January 1, 2005 and January 3, 2004 is as follows (in thousands):

	For the Fiscal Year Ended		
	December 31, 2005	January 1, 2005	January 3, 2004
Contribution .....	\$ 36,384	\$ 42,565	\$ 47,112
Other operating revenue .....	272	353	474
General and administrative expense .....	(8,527)	(9,727)	(10,811)
Stock compensation expense .....	-	(75)	(50)
Other operating expense, net .....	(219)	(396)	(1,015)
Interest expense, net .....	(20,943)	(24,905)	(25,041)
Other income .....	-	1,054	-
Depreciation and amortization .....	(3,976)	(4,053)	(3,753)
Impairment of goodwill and intangible assets .....	(43,707)	-	-
Benefit (provision) for income taxes .....	2,808	(2,254)	(2,403)
Income (loss) from continuing operations .....	(37,908)	2,562	4,513
Income from discontinued operations (net of income taxes of \$0, \$65 and \$458, respectively) .....	-	104	255
Net income (loss) .....	<u>\$ (37,908)</u>	<u>\$ 2,666</u>	<u>\$ 4,768</u>

The fixed assets and inventory of the Company primarily relate to the Company's Great American Cookies manufacturing facility and gifts business segment and related activities. Assets relating to franchising and licensing activity are primarily amounts due from franchisees and licensees and goodwill relating to franchising concepts.

Revenues from franchisees, customers and licensees within the United States were \$86.5 million, \$86.1 million and \$80.6 million or 98.3 percent, 98.9 percent and 98.3 percent of total revenues for the years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively. Revenues from international franchisees, customers and licensees were \$1.5 million, \$1.0 million and \$1.4 million or 1.7 percent, 1.1 percent and 1.7 percent of total revenues for the years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively. Revenues from any single foreign country were not material. Providing geographical information regarding long-lived assets is impracticable.

The Company has one licensee that accounted for \$2.3 million, \$3.1 million and \$3.5 million, or 57.6 percent, 62.7 percent and 63.1 percent of the revenues of the licensing segment for the years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively. The Company has one customer in its gifts business segment that accounted for \$3.6 million, \$4.2 million and \$3.0 million, or 11.8 percent, 16.2 percent and 17.2 percent of revenues of the gifts business segment for the years ended December 31, 2005, January 1, 2005 and January 3, 2004, respectively. There were no other customers or licensees that accounted for more than ten percent of Mrs. Fields' total revenues or any individual segment's revenues.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**Notes to the Consolidated Financial Statements**  
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**10. Discontinued Operations**

TCBY transitioned its equipment sales segment ("Riverport") to a third party equipment and smallwares distributor during the quarter ended March 29, 2003. The distributor purchased certain of Riverport's inventory at cost, subject to certain slow moving inventory purchase price adjustments. The segment's assets that were subject to depreciation and amortization were being periodically expensed over the remaining estimated useful life. The results of operations and financial position of Riverport are classified as discontinued operations in the accompanying consolidated financial statements. The Company does not anticipate any further activity relating to Riverport in future periods

**11. Supplemental Condensed Consolidating Financial Information**

The Senior Secured Notes were issued by the Company and Mrs. Fields Financing Company, Inc., as co-issuers. Mrs. Fields Financing Company, Inc. is a wholly-owned finance subsidiary of Mrs. Fields Famous Brands. The Senior Secured Notes are fully and unconditionally guaranteed on a joint and several basis by all of the Company's domestic subsidiaries other than minor subsidiaries. Mrs. Fields Famous Brands has no independent assets or operations. Therefore, supplemental financial information on a condensed consolidating basis of the guarantor subsidiaries is not required. There are no restrictions on the Company's ability to obtain cash dividends or other distributions of funds from the guarantor subsidiaries, except those imposed by applicable law.

**12. Subsequent Event**

Effective as of March 1, 2006, we entered into an Industrial Net Lease ("Lease") with Natomas Meadows Two, LLC, for the lease of approximately 159,000 square feet of space in Salt Lake City, Utah. Each month during the 120-month initial term under the Lease, commencing on May 1, 2006, the Company is required to remit base rent of \$69,872. The Lease also requires additional payments, including a \$100,000 security deposit, common area maintenance charges, taxes, maintenance and utilities. We will be developing this newly leased space to accommodate our new state-of-the-art gifting operations. This new space will eventually replace approximately 107,000 square feet of space we currently lease in areas throughout Salt Lake City. We will then attempt to terminate the leases for the current space or sublet it. Currently, we anticipate we will open the gifting facility at the new space in the third quarter of 2006.

**MRS. FIELDS FAMOUS BRANDS, LLC**  
**SCHEDULE II – VALUATION AND QUALIFYING ACCOUNTS**

<u>Description</u>	<u>Balance at beginning of period</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at end of period</u>
Allowance for Doubtful Accounts:				
Year ended December 31, 2005 .....	\$ 1,295,000	\$ (74,000)	\$ 609,000	\$ 612,000
Year ended January 1, 2005 .....	<u>\$ 1,948,000</u>	<u>\$ 161,000</u>	<u>\$ 814,000</u>	<u>\$ 1,295,000</u>
Year ended January 3, 2004 .....	<u>\$ 2,434,000</u>	<u>\$ 48,000</u>	<u>\$ 534,000</u>	<u>\$ 1,948,000</u>